

# **Navigating the Complex Skies: A Caveat on Liberalizing Foreign Ownership Restrictions in U.S. Airlines**

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## I. INTRODUCTION

Within a single week in 2008, Aloha Airlines, American Trans Air (ATA), and Skybus Airlines abruptly ceased operations.<sup>1</sup> Smaller carriers EOS Airlines<sup>2</sup> and Champion Air<sup>3</sup> folded within the following two months. Customers scheduled to fly on all of these airlines were left stranded with little to no recourse.<sup>4</sup> Nearly 5,600 employees lost their jobs as a result of these five airlines' closures.<sup>5</sup> Although attributable to a struggling economy and rising fuel costs, this rapid succession of airline closures resulted largely from a lack of adequate capital required to continue operations.<sup>6</sup>

The typical airline suffers through the booms and busts of the economic cycle as any business would. When an established airline fails, however, we as passengers become unfortunate bystanders of the collapse. We may miss the birth of a grandchild, the career-making interview, or the once-in-a-lifetime vacation. When the dominant airline at a major city dissolves, the businesses of that community have to fight to re-gain immediate access to the markets in which they once conducted business. When an airline is healthy,

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<sup>1</sup> *Low-Cost Carrier Skybus Calls It Quits*, MSNBC, Apr. 4, 2008, <http://www.msnbc.msn.com/id/23962964/> [hereinafter *Skybus*].

<sup>2</sup> David Kaminski-Morrow, *All-Premium Carrier Eos Ceases Operations*, FLIGHT INTERNATIONAL, Apr. 28, 2008, <http://www.flightglobal.com/articles/2008/04/28/223307/all-premium-carrier-eos-ceases-operations.html> [hereinafter *Eos*].

<sup>3</sup> Chris Walsh, *Charter Carrier Champion Air Plans to Cease Operations*, ROCKY MOUNTAIN NEWS, Apr. 1, 2008, <http://m.rockymountainnews.com/news/2008/Apr/01/charter-airline-to-shut-down/>.

<sup>4</sup> Skybus instructed its stranded passengers to ask their credit card companies for refunds. See *Skybus*, *supra* note 1.

<sup>5</sup> Data compiled from the following sources: Dave Segal, *Aloha Air Shuts Down*, HONOLULU STAR-BULLETIN, Mar. 31, 2008, <http://archives.starbulletin.com/2008/03/31/news/story01.html>; *Skybus*, *supra* note 1; Walsh, *supra* note 3; Harry R. Weber, *All-Business-Class Niche Airline Eos Folds*, USA TODAY, Apr. 28, 2008, [http://www.usatoday.com/travel/flights/2008-04-27-eos-folds\\_N.htm](http://www.usatoday.com/travel/flights/2008-04-27-eos-folds_N.htm).

<sup>6</sup> See *infra* Part III.A.

businesses expand, families reunite, and diplomatic ties are rekindled. In the end, a stable and healthy air transport system contributes to the global connections that bind us together as societies.

U.S. carriers require enormous capital to operate, and because federal laws limit their ownership and control to U.S. citizens, the source of that capital has far-reaching implications. If the U.S. is suffering adverse economic conditions, U.S. capital is scarce, but allowing foreign ownership in U.S. airlines makes available new sources of capital and likely allows foreign investors to rescue ailing U.S. carriers. Proponents of restrictions on foreign ownership cite concerns about safety, domestic employment, and national defense, and for the most part, Congress has listened. While recent events in the airline industry seem to suggest that these generalized anxieties are unfounded, potential risks to national defense exist. With regard to national defense risks, what the United States fears should not be whether a foreign private entity takes control of a U.S. airline but whether a foreign government takes such control.

This Note will first discuss the background and purposes of foreign ownership restrictions, including the method by which the U.S. Department of Transportation polices these restrictions. While outlining this background, this Note will address the history of bilateral aviation agreements that govern air services between two countries, including the wave of liberal “Open Skies agreements” enacted by the U.S. beginning in the 1990s. Part III details the arguments for and against liberalizing the foreign investment restrictions in U.S. airlines, dispelling arguments made against liberalization based on safety and employment while emphasizing issues of national defense and the Civil Reserve Air Fleet Program (CRAF). In doing so, the Note discusses the U.S.-EU Open Skies Agreement, which partially liberalizes air travel between the U.S. and European Union states. Part IV argues that given circumstances specific to most EU countries and the agreement between the U.S. and EU, any relaxation of foreign ownership restrictions should be initially tailored to EU nations. This Note also cautions against unsupervised liberalization of the restrictions and proposes that the Department of Transportation continue to monitor ownership structures of U.S. airlines to ensure that non-EU nations and other foreign governments do not exert control over U.S. airlines. The possibility of foreign government ownership poses the primary threat to the Department of Defense’s Civil Reserve Air Fleet Program.

## II. BACKGROUND

### A. History of the Statutory Foreign Ownership Restrictions

Congress began regulating the burgeoning air travel industry with its passage of the Air Commerce Act of 1926. Among its myriad provisions, the Air Commerce Act of 1926 required that U.S. citizens hold at least 51% ownership in U.S. carriers and occupy at least two-thirds of a U.S. carrier's board director positions in order to possess aircraft registered in the U.S.<sup>7</sup> The House Report notes that these restrictions were in place to enable U.S.-registered aircraft to receive "the protection of [the U.S.] flag when abroad,"<sup>8</sup> while at the same time limiting the "exclusive privilege" of domestic air commerce to U.S.-owned aircraft.<sup>9</sup> Some have also suggested that one motivation behind the restriction was to prevent foreign governments from using U.S. aircraft as war instruments.<sup>10</sup> Congress further refined control with respect to U.S. airlines by enacting the Civil Aeronautics Act of 1938, which required U.S. citizens to control 75% of a domestic airline's voting stock.<sup>11</sup> By means of a 2003 amendment,<sup>12</sup> Congress expanded the statute to clarify that an airline is a U.S. citizen if it is "under the actual control of citizens of the United States"; this language is included in the statute's current form.<sup>13</sup>

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<sup>7</sup> Pub. L. No. 69-254, §§ 3(a), 9(a), 44 Stat. 568 (1926).

<sup>8</sup> H.R. REP. NO. 69-572, at app. § 2(A) (1926), *reprinted in* CIVIL AERONAUTICS, LEGISLATIVE HISTORY OF THE AIR COMMERCE ACT OF 1926, at 34 (1928).

<sup>9</sup> *Id.* Prior to the Act, the U.S. had already agreed to nationality requirements with regard to aircraft registration under article 7 of the Convention Relating to International Air Navigation in 1919, of which the U.S. was a signatory with reservations. Convention Relating to International Air Navigation, art. 7, Oct. 13, 1919, *reprinted in* CIVIL AERONAUTICS, LEGISLATIVE HISTORY OF THE AIR COMMERCE ACT OF 1926, at 159 (1928) ("No aircraft shall be entered on the register of one of the contracting States unless it belongs wholly to nationals of such State.").

<sup>10</sup> See Bimal Patel, *A Flight Plan Towards Financial Stability—The History and Future of Foreign Ownership Restrictions in the United States Aviation Industry*, 73 J. AIR L. & COM. 487, 488–489 (2008) (noting how the U.S. sought to prevent the German government from acquiring U.S. aircraft).

<sup>11</sup> Pub. L. No. 75-706, § 1107(i)(6), 52 Stat. 973 (1938); *see* Patel, *supra* note 10, at 489 (attributing the percentage increase to Depression-era protectionism).

<sup>12</sup> Congress passed the amendment in 2003 as part of Vision 100—Century of Aviation Reauthorization Act, Pub. L. No. 108-176, § 807 (2003).

<sup>13</sup> 49 U.S.C. § 40102(a)(15)(C) (2006). At the time of this writing, Congress has been considering an FAA reauthorization bill that would, in fact, strengthen foreign control restrictions as opposed to liberalizing them. H.R. 915, 111th Cong. § 801 (2009). The bill clarifies "actual control" as requiring U.S. citizen control over "all matters pertaining to the business and structure of the air carrier, including operational matters

In the early 1990s and the early 2000s—periods during which the U.S. airline industry experienced significant financial difficulties—two presidential administrations considered the possibility of loosening the foreign ownership restrictions to stabilize the industry. In 1992, the U.S. General Accounting Office (GAO) issued its first report on the control and investment restrictions governing U.S. airlines.<sup>14</sup> The report noted that four principal reasons motivated the restrictions: “(1) protection of the heavily subsidized fledgling airline industry, (2) regulation of international air service through bilateral agreements negotiated with foreign governments, (3) concern about allowing foreign aircraft access to U.S. airspace, and (4) military reliance on civilian airlines to supplement airlift capacity.”<sup>15</sup> The first and third concerns are more easily dismissed in the current industry environment than they were several decades ago; the airline industry is no longer “fledgling,” and an abundance of foreign aircraft enter U.S. airspace everyday to reach U.S. destinations.<sup>16</sup>

### *B. The Department of Transportation’s Regulation of Foreign Ownership*

The Department of Transportation (DOT) plays a key role in determining whether a U.S. carrier has met its U.S. ownership obligations in order to be certified to operate.<sup>17</sup> DOT has interpreted citizen control to mean “day-to-day management decisions made by U.S. citizens,”<sup>18</sup> which colors DOT’s determination of citizenship despite an airline’s ability to meet the threshold percentage for U.S. ownership.<sup>19</sup> DOT evaluates whether U.S. citizens have

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such as marketing, branding, fleet composition, route selection, pricing, and labor relations.” *Id.*

<sup>14</sup> U.S. GEN. ACCOUNTING OFFICE, AIRLINE COMPETITION – IMPACT OF CHANGING FOREIGN INVESTMENT AND CONTROL LIMITS ON U.S. AIRLINES 1 (1992) [hereinafter GAO 1992].

<sup>15</sup> *Id.* at 12–13.

<sup>16</sup> See, e.g., Press Release, Bureau of Transp. Statistics, Summary 2008 Traffic Data for U.S and Foreign Airlines: Total Passengers Down 3.5 Percent from 2007, Apr. 23, 2009, [available at](http://www.bts.gov/press_releases/2009/bts019_09/html/bts019_09.html) [http://www.bts.gov/press\\_releases/2009/bts019\\_09/html/bts019\\_09.html](http://www.bts.gov/press_releases/2009/bts019_09/html/bts019_09.html) (finding that both U.S. and foreign carriers operated 10.7 million domestic and international flights involving a U.S. airport in 2008).

<sup>17</sup> 14 C.F.R. § 119.33 (2010) (requiring U.S. citizenship for air carriers and commercial passenger or cargo operations).

<sup>18</sup> U.S. GEN. ACCOUNTING OFFICE, ISSUES RELATING TO FOREIGN INVESTMENT AND CONTROL OF U.S. AIRLINES 2 (2003) [hereinafter GAO 2003].

<sup>19</sup> See Patel, *supra* note 10, at 490–91 (discussing Willye Peter Daetwyler, 58 C.A.B. 118 (1971)). The case involved a carrier whose control was scrutinized even when it had met the statutory requirements for U.S. ownership. In the view of the Civil

actual control over an airline on a case-by-case basis, analyzing both contractual agreements and corporate structure.<sup>20</sup> DOT and its predecessor agencies have been reluctant to find U.S. citizenship when a foreign entity could merely exert influence over the carrier's decisions.<sup>21</sup>

By the 1990s, the world political environment left the U.S. without a clear military enemy or rival, thereby weakening some of the 1926 reasoning for protective measures on foreign ownership. DOT nevertheless continued its restrictive stance on foreign investment in U.S. carriers, maintaining the position that any foreign ability to influence a carrier's decision would result in a revocation of the U.S. citizenship of the carrier. A deal between British Airways and US Air<sup>22</sup> in the early 1990s, for example, was potentially problematic because the agreement would have allowed British Airways-appointed board members on US Air's board to veto decisions made by other board members.<sup>23</sup> After the two sides made some necessary changes to the agreement, DOT allowed the transaction to proceed.<sup>24</sup>

Just prior to the British Airways-US Air deal, Northwest Airlines (Northwest) entered into a merger agreement with Wings Holdings (Wings),

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Aeronautics Board (one of the governing agencies at the time), the carrier needed to prove that the "substance of the transaction [was] in accordance with the policy." *Id.* at 491.

<sup>20</sup> *Id.*

<sup>21</sup> See *Intera Arctic Servs. Inc.*, 1987 DOT Av. LEXIS 337, at \*9 (Aug. 18, 1987); see also Patel, *supra* note 10, at 495 (citing *In re The Citizenship of DHL Airways*, 2004 DOT Av. LEXIS 404, at \*22 (May 13, 2004)). However, DOT has not seemed as active in shielding U.S. airlines from foreign influence with regard to contractual obligations arising from debt agreements. See, e.g., Micheline Maynard, *US Airways and America West Plan to Merge*, N.Y. TIMES, May 20, 2005, <http://www.nytimes.com/2005/05/20/business/20air.html?pagewanted=1&r=1> (noting how Airbus SAS, a subsidiary of European plane manufacturer EADS, provided a \$250 million loan to US Airways in return for US Airways' decision to purchase new Airbus aircraft in the future); see also A. Michael Froomkin, *Reinventing the Government Corporation*, 1995 U. ILL. L. REV. 543, 569 (1995) ("A valid distinction exists between a corporation in which the federal government has taken an active role in management or control, and a corporation in which the government finds itself temporarily holding the debt or equity of a going concern . . ."). A discussion of the challenges posed by government ownership in the airline industry follows in Part III.D.2.

<sup>22</sup> US Air changed its name to US Airways in 1996 subject to a rebranding strategy under the direction of CEO Stephen Wolf. Suzanne Wooton, *USAir Announces New Look, Name Change to US Airways*, BALTIMORE SUN, Nov. 13, 1996, at 1C.

<sup>23</sup> Patel, *supra* note 10, at 493.

<sup>24</sup> ISABELLE LELIEUR, LAW AND POLICY OF SUBSTANTIAL OWNERSHIP AND EFFECTIVE CONTROL OF AIRLINES 38 (2003). The alliance lasted for several years but was discontinued in 1997 when it became apparent that the deal did not function as both sides had hoped. GAO 2003, *supra* note 18, at 6.

a private investment company.<sup>25</sup> DOT had ordered the parties to submit information testifying to Northwest's continued fitness and citizenship as a U.S. carrier.<sup>26</sup> DOT found that nearly two-thirds of Wings' voting stock was owned by U.S. citizens; this block was able to appoint a majority of Wings' board.<sup>27</sup> KLM, the flag carrier for the Netherlands, had also heavily invested in Wings, having purchased \$350 million in preferred stock and \$50 million in common stock, with an option to purchase additional common voting stock.<sup>28</sup> KLM, in addition to its ownership of 5% voting stock, had the right to appoint one member to Wings' board and the right to establish a three-member committee to advise Northwest on its financial affairs.<sup>29</sup> Because DOT was concerned about KLM's ability to exert control over Wings, DOT compelled KLM to significantly reduce its share of equity, as well as its access to sensitive information relating to Northwest's affairs.<sup>30</sup> Additionally KLM was forced to forgo its right to establish a financial advisory committee.<sup>31</sup> DOT's treatment of Wings was not based on the statutory requirements for Wings' U.S. citizenship, which were met given the statutory text at the time<sup>32</sup>, but, rather, DOT was concerned about KLM exerting "actual control" over the U.S. carrier Northwest through its investment in Wings.<sup>33</sup> DOT later reconsidered the Wings case and allowed a modified arrangement between Northwest and KLM to proceed, following an Open Skies Agreement between the U.S. and the Netherlands.<sup>34</sup>

Gradually through the late 1990s and 2000s, DOT began to rule more favorably on deals involving foreign investment. During the mid 2000s, U.K. mogul Sir Richard Branson sought to expand his Virgin Group brand (Virgin) by incorporating a new U.S.-based carrier, eventually named Virgin

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<sup>25</sup> DEP'T OF TRANSP., ACQUISITION OF NORTHWEST AIRLINES BY WINGS HOLDINGS, INC., DOT ORDER NO. 89-9-51, DOCKET NO. 46371 (Sept. 29, 1989).

<sup>26</sup> *Id.*

<sup>27</sup> *Id.* at 2.

<sup>28</sup> *Id.*

<sup>29</sup> *Id.* at 3.

<sup>30</sup> *Id.* at 3-4.

<sup>31</sup> DEP'T OF TRANSP., *supra* note 25, at 3.

<sup>32</sup> See *supra* text accompanying note 12, relating to the 2003 amendment requiring U.S. citizens exert "actual control." During the time period of the Wings deal, this language was not in the statute.

<sup>33</sup> DEP'T OF TRANSP., *supra* note 25, at 4-5 ("Analysis in this area has always necessarily been on a case-by-case basis, as there are myriad potential avenues of control. The control standard is a *de facto* one—we seek to discover whether a foreign interest may be in a position to exercise actual control over the airline, *i.e.*, whether it will have a substantial ability to influence the carrier's activities.").

<sup>34</sup> See *infra* note 74 and accompanying text.

America.<sup>35</sup> Branson had helped to develop similar Virgin-brand airlines in other parts of the world, including Australia and Nigeria, with mixed success.<sup>36</sup> Due to Virgin America's close ties to the Virgin Group at its inception, DOT officials were initially concerned about the amount of control Branson and Virgin would exert over the U.S. carrier.<sup>37</sup> In an order dated December 27, 2006, DOT found that Virgin America had failed to establish that it would meet the requisite U.S. control requirements in order to qualify as a U.S. citizen under the Federal Aviation Act.<sup>38</sup> Despite Virgin America's 75% voting control by a Delaware investment company (VAI) and its predominantly U.S.-citizen management staff, DOT (on the urging of U.S. carriers Continental Airlines, Delta Air Lines, United Airlines, Northwest Airlines, US Airways, and American Airlines at various times during the proceedings) determined that actual control of Virgin America was held by foreign citizens.<sup>39</sup> Its decision noted the close ties the airline and its management would have with Virgin and Branson, as well as the fact that VAI's individual investors were found to be influenced by foreign entities.<sup>40</sup> DOT did, however, leave the door open to future evidence proving Virgin America's citizenship.<sup>41</sup> In response, Virgin America made what DOT characterized as "material changes" to its debt financing structure and board composition such that DOT was satisfied and declared Virgin America a U.S.

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<sup>35</sup> Dan Reed, *Branson Flies Under the Radar as Virgin America Takes Off*, USA TODAY, Aug. 8, 2007, at B1 (emphasizing Virgin America's Virgin roots).

<sup>36</sup> Virgin sought to sell a 49% stake in Nigeria Eagle Airways (formerly Virgin Nigeria) following financial difficulties and a dispute with the Nigerian government. Matthew Green, *Virgin in Talks to Sell Out of Nigeria*, FIN. TIMES, Aug. 19, 2008, <http://www.ft.com/cms/s/0/ceb26f6e-6e17-11dd-b5df-0000779fd18c.html#axzz1FJGHCFG0>. Australian carrier Virgin Blue is not only profitable, but rapidly expanding. Geoffrey Thomas, *Virgin Blue Celebrates Half-Year Profit with Commitment for 50 737s*, ATW DAILY NEWS, Feb. 25, 2010, [atwonline.com/airline-finance-data/news/virgin-blue-celebrates-half-year-profit-commitment-50-737s-0427](http://atwonline.com/airline-finance-data/news/virgin-blue-celebrates-half-year-profit-commitment-50-737s-0427).

<sup>37</sup> Reed, *supra* note 35.

<sup>38</sup> DEP'T OF TRANSP., APPLICATION OF VIRGIN AMERICA, INC. – ORDER TO SHOW CAUSE, DOT ORDER NO. 2006-12-23, DOCKET NO. OST-2005-23307 (Dec. 27, 2006).

<sup>39</sup> *Id.*

<sup>40</sup> *Id.* at 15; *see also id.* at 16–20 (finding that actual control of Virgin America would be in the hands of foreign citizens based on the following: "1. Virgin Group's extensive influence over [Virgin America's] management . . . 2. Virgin Group's pervasive involvement in the creation of Virgin America . . . 3. [f]unding provided by the Virgin Group . . . 4. [t]he Virgin Trademark License Agreement . . . 5. [the fact that] approval and/or consent of the Virgin Group must be obtained prior to certain changes contemplated by Virgin America and VAI").

<sup>41</sup> *Id.* at 20.



citizen, granting it certification as a U.S. carrier.<sup>42</sup> Virgin America also successfully assured DOT that a restructuring of VAI's control structure would negate influence by foreign entities.<sup>43</sup>

Virgin America's citizenship came under scrutiny again in 2009 when Alaska Airlines, citing a *Wall Street Journal* report suggesting that two of VAI's controlling entities had surrendered economic rights back to Virgin, filed a petition for a public proceeding. It claimed that Virgin America had lost its U.S. citizenship status.<sup>44</sup> By this point, Virgin America had operated flights across the U.S. for over two years.<sup>45</sup> DOT dismissed Alaska Airlines' petition in January 2010,<sup>46</sup> noting that new U.S. investors had contributed personal assets in acquiring full control of VAI, among other changes to Virgin America's control structure.<sup>47</sup> DOT was satisfied that these investors had "greater incentive to actively participate in the strategic decisions of Virgin America."<sup>48</sup>

DOT also ruled favorably on an investment by German corporation Deutsche Lufthansa AG (Lufthansa) in U.S.-based JetBlue Airways Corporation (JetBlue), which gained approval in 2008.<sup>49</sup> Lufthansa acquired

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<sup>42</sup> DEP'T OF TRANSP., APPLICATION OF VIRGIN AMERICA, INC. – FINAL ORDER, DOT ORDER NO. 2007-5-11, DOCKET NO. OST-2005-23307 (May 18, 2007).

<sup>43</sup> *Id.*

<sup>44</sup> DEP'T OF TRANSP., ALASKA AIRLINES, INC. – RENEWED MOTION OF ALASKA AIRLINES, INC. FOR A PUBLIC PROCEEDING, DOCKET NO. OST-2009-0037 (Aug. 21, 2009).

<sup>45</sup> See Press Release, Virgin America Inc., Virgin America Takes to the Skies (Aug. 8, 2007), <http://www.virginamerica.com/va/press/2007/Aug/Takes-to-the-Skies.html> (noting the inauguration date of August 8, 2007); DEP'T OF TRANSP., *supra* note 44 (dated August 21, 2009).

<sup>46</sup> DEP'T OF TRANSP., APPLICATION OF VIRGIN AMERICA, INC. – ORDER DISMISSING PETITIONS, DOT ORDER NO. 2010-1-5, DOCKET NO. OST-2005-23307 (Jan. 8, 2010) ("We are not persuaded that the public interest requires us to institute a public proceeding in this matter. . . . [I]t has long been the Department's practice to conduct continuing fitness reviews informally. We have determined that an informal continuing fitness review is appropriate here. We have completed such a review of Virgin America's fitness, and have concluded that Virgin America remains a U.S. citizen, subject to certain conditions.").

<sup>47</sup> Business Review Letter from Susan Kurland, Assistant Sec'y for Aviation & Int'l Affairs, Dep't of Transp., to Kenneth Quinn, Pillsbury Winthrop Shaw Pittman LLP, Counsel for Virgin America Inc. (Jan. 8, 2010), available at <http://ostpxweb.dot.gov/aviation/busrevletters/Virgin%20America%20Letter.pdf> [hereinafter DOT Virgin Letter].

<sup>48</sup> *Id.*

<sup>49</sup> Business Review Letter from Lauralyn Remo, Acting Chief, Air Carrier Fitness Div., Dep't of Transp., to Jonathan Hill, Dow Lohnes PLLC, Counsel for JetBlue Airways Corp. (Jan. 22, 2008),

42 million newly issued common shares of JetBlue, or 19% of JetBlue's equity.<sup>50</sup> The investment brought roughly \$300 million to JetBlue, while Lufthansa gained one seat on JetBlue's board of directors<sup>51</sup> with the possibility of adding a second seat a year following the close of the transaction.<sup>52</sup> DOT determined that JetBlue would retain its U.S. citizenship status under the agreement, though it reserved the right to change its determination in light of any substantial changes to JetBlue's corporate ownership.<sup>53</sup>

DOT has articulated fewer concerns when an airline offers its shares to the public. When now-defunct<sup>54</sup> MAXjet Airways, Inc. (MAXjet) proposed an initial public offering (IPO) in the mid-2000s, DOT approved the airline's self-enforcement proposals for adhering to foreign investment restrictions.<sup>55</sup> MAXjet planned to review the citizenship of any holder of its voting stock and to immediately remove voting rights from any shares that would bring total foreign control to greater than 25%.<sup>56</sup> To accommodate this, investors from countries without Open Skies agreements<sup>57</sup> with the U.S. would be compelled to sell their shares within 90 days if their shares would bring foreign control to 25% or higher.<sup>58</sup> Under MAXjet's proposal, foreign non-voting equity ownership would be allowed up to 50%, with any additional foreign investors forced to sell their shares within 90 days.<sup>59</sup> MAXjet indicated that it would conduct the sale itself if such criteria were met and foreign investors refused to sell their shares.<sup>60</sup> As in the case of JetBlue, DOT required MAXjet to inform the department of any substantial changes to the

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<http://ostpxweb.dot.gov/aviation/busrevletters/Ownership%20Approval%20Letter.pdf> [hereinafter DOT JetBlue Letter].

<sup>50</sup> Press Release, Deutsche Lufthansa AG, Lufthansa to Make Equity Investment in JetBlue; Will Buy up to 19% Stake for \$7.27 per Share (Dec. 13, 2007), [http://www.lufthansa.com/mediapool/pdf/86/media\\_492286.pdf](http://www.lufthansa.com/mediapool/pdf/86/media_492286.pdf).

<sup>51</sup> *Id.*

<sup>52</sup> DOT JetBlue Letter, *supra* note 49.

<sup>53</sup> *Id.*

<sup>54</sup> MAXjet terminated operations on December 24, 2007. *Maxjet Airways Ceases Operations*, BUSINESS TRAVEL NEWS, Dec. 24, 2007, [http://www.btnonline.com/businesstravelnews/search/article\\_display.jsp?vnu\\_content\\_id=1003688400](http://www.btnonline.com/businesstravelnews/search/article_display.jsp?vnu_content_id=1003688400).

<sup>55</sup> Business Review Letter from Andrew Steinberg, Assistant Sec'y for Aviation and Int'l Affairs, Dep't of Transp., to William Kutzke, Gen. Counsel, MAXjet Airways, Inc. (Mar. 12, 2007) [hereinafter DOT MAXjet Letter].

<sup>56</sup> *Id.* at 1.

<sup>57</sup> See *infra* notes 73–74 and accompanying text.

<sup>58</sup> DOT MAXjet Letter, *supra* note 55, at 2.

<sup>59</sup> *Id.*

<sup>60</sup> *Id.*

ownership structure, and DOT reserved the right to reject MAXjet's fitness should the changes fail to meet foreign ownership restrictions.<sup>61</sup>

### *C. The International Aviation Environment: Bilateralism and Open Skies*

The global landscape for international carriers is primarily characterized as a series of bilateral agreements negotiated between pairs of countries.<sup>62</sup> These agreements establish particular rights to each party of the negotiation, including rights of access benefiting each party's air carriers.<sup>63</sup> A country engaged in such an agreement exerts sovereignty over the air traffic over its territory by retaining the option to refuse rights to those countries that refuse to grant reciprocal benefits or to foreign carriers that refuse to comply with the country's regulations.<sup>64</sup> Restricting foreign ownership in one country's airlines was one method for countries to enforce these bilateral agreements, or at least, to continue to benefit from the route authorities afforded to its airlines under one of these agreements.<sup>65</sup>

The restrictiveness of such agreements varied during the past couple decades, typically specifying in detail the capacity and frequency of air

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<sup>61</sup> *Id.* at 2–3.

<sup>62</sup> MAREK ZYLICZ, INTERNATIONAL AIR TRANSPORT LAW 135 (1992).

<sup>63</sup> The ability to provide air services to a foreign country is not a default right; special permission must be granted by the foreign country. MICHAEL MILDE, ESSENTIAL AIR AND SPACE LAW 100 (2008).

<sup>64</sup> See, e.g., Federal Aviation Act of 1958, Pub. L. No. 85-726, § 1108(b), 72 Stat. 731, now codified and amended as 49 U.S.C. § 41703(a) (“A [non-military] foreign aircraft . . . may be navigated in the United States . . . if the country of registry grants a similar privilege to aircraft of the United States . . .”). The text, though not from a bilateral agreement itself, exemplifies the desire for reciprocal benefits that can accompany bilateral arrangements: one country grants access to a foreign carrier as long as the foreign carrier's country grants access to the first country's carriers, as an example.

<sup>65</sup> LELIEUR, *supra* note 24, at 7. Suppose a bilateral agreement between the U.S. and China provided that only two U.S. airlines could fly into Shanghai's Pudong International Airport. While the U.S. airlines are under the control of U.S. citizens, the U.S. benefits from the bilateral agreement. If, on the other hand, China or another foreign country assumed control of the U.S. airlines, then the U.S. no longer could control the airlines intended to provide the U.S.-Shanghai service. For one, a foreign, non-Chinese company that purchases control of the U.S. airline may be barred from operating the U.S.-Shanghai service because its home country was not a party to the agreement between the U.S. and China. In a different vein, if a Chinese company purchased both U.S. airlines operating the U.S.-Shanghai route, then Chinese companies would effectively control all U.S.-Shanghai service, eliminating the benefits the U.S. would receive under the bilateral agreement.

services between the two countries, among other provisions.<sup>66</sup> One of the well-known restrictive agreements in recent history was Bermuda II, which governed air traffic between the United States and the United Kingdom. Bermuda II, itself a revision of a less restrictive Bermuda I,<sup>67</sup> limited, among other things, air service between the U.S. and London's lucrative Heathrow Airport to two carriers from each country.<sup>68</sup> In the aforementioned case of British Airways' investment in US Air, competing U.S. carriers successfully challenged the proposed British Airways transaction by noting that Bermuda II prevented U.S. investors from investing in any British carriers, thereby denying U.S. carriers the same level of access to the U.K. market as British Airways would receive in the U.S. market through US Air.<sup>69</sup> Nevertheless an altered arrangement between British Airways and US Air did pass DOT scrutiny, with the agreement and all investments later discontinuing in 1997.<sup>70</sup>

Bilateral restrictions in U.S. agreements loosened in the early 1990s when DOT actively sought Open Skies agreements with other nations.<sup>71</sup> DOT's new initiative targeted Europe, which was experiencing increased economic liberalization between the various European states at the time.<sup>72</sup> The goal of Open Skies agreements is to make international aviation markets accessible to the U.S., undoing traffic and capacity restrictions that characterized previous bilateral agreements.<sup>73</sup> The U.S.'s first Open Skies agreement was signed in 1992 with the Netherlands as a condition for DOT approval of the Northwest-KLM alliance proposal under review.<sup>74</sup>

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<sup>66</sup> ZYLICZ, *supra* note 62, at 142.

<sup>67</sup> *Id.*

<sup>68</sup> *Bermuda II Initialled*, FLIGHT INTERNATIONAL, Jul. 2, 1977, at 5. The process of designating two carriers from each country to operate a route was referred to as "dual designation." At the time of Bermuda II's signing, Laker Airways and B.CAL were the British carriers granted permission to operate the London-New York route, and Pan Am and TWA were the two American carriers granted the same route authority . . . *Id.*

<sup>69</sup> Patel, *supra* note 10, at 494.

<sup>70</sup> *British Airways Disposes of Last US Airways Stock*, N.Y. TIMES, May 22, 1997, at D4.

<sup>71</sup> Seth M. Warner, *Liberalize Open Skies: Foreign Investment and Cabotage Restrictions Keep Noncitizens in Second Class*, 43 AM. U. L. REV. 277, 299 (1993).

<sup>72</sup> Defining "Open Skies," 57 Fed. Reg. 19323-01 (May 5, 1992).

<sup>73</sup> *Id.* Specifically the DOT order sought Open Skies agreements that would, among other things, provide "(1) open entry on all routes; (2) Unrestricted capacity and frequency on all routes; (3) Unrestricted route and traffic rights, that is, the right to operate service between any point in the United States and any point in the European country . . . (8) Open code-sharing opportunities." *Id.*

<sup>74</sup> LELIEUR, *supra* note 24, at 28.

Since then nearly 100 countries have signed Open Skies agreements with the U.S.<sup>75</sup> By early 2007, the U.S. had negotiated Open Skies agreements with nearly twenty European countries, approximately three-quarters of whom were EU member states.<sup>76</sup> On April 30, 2007, the U.S. and EU signed an air transport agreement that served as an Open Skies Agreement between the twenty-seven EU member states and the U.S.<sup>77</sup> The agreement broadly made available new air routes between the U.S. and EU member countries, allowing airlines from the U.S. to fly from any U.S. city to any EU member city, and vice versa.<sup>78</sup>

While a significant step toward full liberalization, the agreement maintains restrictions in a number of areas. U.S. airlines, for example, can commercially fly between any two EU member states, but cabotage—the ability to commercially operate a domestic route in a foreign country—for both U.S. and EU carriers is forbidden within any EU state or the U.S., respectively.<sup>79</sup> The agreement also briefly addresses ownership restrictions. For EU airlines and other investors, the U.S. foreign ownership restrictions on equity investment and control remain in place, while for U.S. investors, EU foreign ownership restrictions apply, requiring majority ownership and control by EU citizens.<sup>80</sup> EU member states also reserve the right to restrict foreign ownership in their airlines to the standards adhered to in the U.S.<sup>81</sup>

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<sup>75</sup> *Open Skies Partners*, U.S. DEPARTMENT OF STATE, <http://www.state.gov/e/eeb/rls/othr/ata/114805.htm>.

<sup>76</sup> *Id.*

<sup>77</sup> Air Transport Agreement, 2007 O.J. (L 134) 4 [hereinafter U.S.-EU Agreement].

<sup>78</sup> *Id.* art. 3, § 1(c)(i)–(ii) (“[Each party grants the other] the right to perform international air transportation between points on the following routes: (i) for airlines of the United States (hereinafter US airlines), from points behind the United States via the United States and intermediate points to any point or points in any Member State or States and beyond; . . . (ii) for airlines of the European Community and its Member States (hereinafter Community airlines), from points behind the Member States via the Member States and intermediate points to any point or points in the United States and beyond . . .”).

<sup>79</sup> *Id.* art. 3(6). For example, EU airlines do not have permission to commercially fly between a U.S. city such as Chicago and another U.S. city such as Denver. U.S. airlines do not have permission to commercially fly between the two Spanish cities of Madrid and Barcelona, but they do have permission to fly between Madrid and a city in another EU member state, such as Frankfurt.

<sup>80</sup> *Id.* Annex 4, art. 1(1)–(2).

<sup>81</sup> *Id.* Annex 4, art. 1(4) (“Notwithstanding paragraph 2, the European Community and its Member States reserves the right to limit investments by US nationals in the voting equity of a Community airline made after the signature of this Agreement to a level equivalent to that allowed by the United States for foreign nationals in US airlines, provided that the exercise of that right is consistent with international law.”).

The 2007 agreement was amended on June 24, 2010 without substantial changes to existing ownership provisions.<sup>82</sup>

### III. BALANCING THE BENEFITS OF INCREASED FOREIGN INVESTMENT WITH ITS RISKS

As the introduction to this Note states, increased foreign investment would not only provide beneficial effects to U.S. airlines—it may allow them to survive. Liberalization of ownership restrictions is also more in line with American ideals of free market capitalism.<sup>83</sup> However, the positive effects of liberalized ownership restrictions must be fairly balanced by arguments made against such liberalization. To this end, the following sections consider both the need and the risks of foreign ownership liberalization. The need for capital is balanced by concerns about standards of safety, domestic employment, and national defense. Although the following sections find that concerns about safety and employment are outweighed by the need for liberalization, this Note finds that the risk to national defense posed by liberalization is significant.

#### A. *The Benefit: The Need for Capital*

Airlines live and die off of the ability to acquire capital.<sup>84</sup> Because of the enormous sums of capital required to run the operations of an airline—let alone start up or expand an airline—adequate financing is a regulatory requirement for any airline in the U.S.<sup>85</sup> Airlines benefit financially from

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<sup>82</sup> Protocol To Amend the Air Transport Agreement Between the United States of America and the European Community and Its Member States, Signed on April 25 & 30, 2007, Protocol, June 24, 2010 [hereinafter U.S.-EU Amended Agreement], *available at* <http://www.state.gov/documents/organization/143930.pdf> (refusing to impose mandatory changes to Annex 4 of the original agreement, which discussed ownership restrictions).

<sup>83</sup> See, e.g., Patel, *supra* note 10, at 522 (“[F]ree market economic principles dictate that private enterprises in the United States be given maximum choice in commercial decisions.”).

<sup>84</sup> See, e.g., discussion on the financial bailout of America West Airlines, *infra* notes 172–73 and accompanying text; see also Patel, *supra* note 10, at 508 (noting the collapse of several airlines around the world, including Swissair, Sabena of Belgium, and Ansett Australia, who were unable to acquire new sources of investment capital); *infra* notes 99–102 and accompanying text.

<sup>85</sup> 14 C.F.R. § 119.36(e) (2010) (FAA regulations requiring submission of recent and projected financial data before the issuance of certification to start up operations as a commercial air carrier). DOT also publishes its own financial requirements for starting up an air carrier. DEPARTMENT OF TRANSPORTATION, HOW TO BECOME A CERTIFICATED AIR CARRIER 17–21 (2005), *available at* <http://ostpxweb.dot.gov/aviation/certific/Certificated%20packet2.pdf>.

foreign investment, particularly at times when domestic investment is decreased by a domestic recession and the airline is unable to raise sufficient capital.<sup>86</sup> Airlines have large capital needs that begin before the start of operations and continue on a periodic basis throughout an airline's lifetime.<sup>87</sup> As an industry, airlines have capital needs that have only grown over time.<sup>88</sup> The most obvious start-up cost is the airline's aircraft, which, alongside the multi-hundred million dollar investment if purchased outright,<sup>89</sup> require spare parts and equipment. Airlines often reduce the costs of acquiring aircraft through leasing arrangements,<sup>90</sup> though leasing still requires significant capital in the aggregate if an airline aspires to rapidly expand its fleet. Much of these start-up costs are financed by debt, but airlines often seek equity capital to start up and expand, especially during times of tight or expensive credit.

JetBlue, as an example, was considered a well-capitalized airline at its founding, drawing in \$467 million of equity capital in its first four years of operation.<sup>91</sup> The airline also had debt of \$1.11 billion, with an additional \$6.58 billion secured for the purchase of equipment including 199 aircraft over eight years.<sup>92</sup> Despite the significant capital secured during the airline's inception, JetBlue's heavy reliance on debt financing was disadvantageous, since the excessive debt could adversely affect the airline's ability to secure future debt financing for expected expansions and the debt obligations could divert cash from the airline's operations and generate significant costs from interest rate fluctuations.<sup>93</sup>

Airlines require new aircraft to maintain and expand their route networks. Fleet replacement and expansion is a continuous process. As airlines grow,

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<sup>86</sup> Patel, *supra* note 10, at 508.

<sup>87</sup> LELIEUR, *supra* note 24, at 69.

<sup>88</sup> Patel, *supra* note 10, at 507 ("According to a 1990s study, the world's airlines have capital needs of around \$815 billion as compared to \$147 billion ten years ago.") (citing LELIEUR, *supra* note 24, at 70 n.39).

<sup>89</sup> Aircraft, if purchased new, typically cost between \$50 million and \$300 million. JetBlue's start-up aircraft, the Airbus A320, for example, averaged \$76.9 million in 2008. *Airbus Aircraft Range of 2008 List Prices*, AIRBUS SAS, [http://www.airbus.com/store/mm\\_repository/pdf/att00011726/media\\_object\\_file\\_ListPrices2008.pdf](http://www.airbus.com/store/mm_repository/pdf/att00011726/media_object_file_ListPrices2008.pdf) (last visited Feb. 28, 2011).

<sup>90</sup> See Leslie Wayne, *The Real Owner of All Those Planes*, N.Y. TIMES, May 10, 2007, at C1 ("Airlines lease airplanes for the same reason that cash-short consumers lease cars—they can get new models for lower payments.").

<sup>91</sup> JetBlue Airways Corp., Annual Report (Form 10-K) 5 (Feb. 11, 2004) [hereinafter JetBlue 2003 Annual Report], available at <http://library.corporate-ir.net/library/13/131/131045/items/211509/0310kb.pdf>.

<sup>92</sup> *Id.* at 22.

<sup>93</sup> *Id.*

they require additional aircraft to increase flight frequencies on existing routes and to open up new destinations within their networks. In 2003, for example, JetBlue had firm orders for nearly 200 aircraft, to be delivered at a rate of between nine and thirty aircraft per year.<sup>94</sup> In contrast, airlines like AirTran Airways deferred delivery of aircraft when capital was scarce due to record high fuel costs.<sup>95</sup>

At the same time, aircraft maintenance costs increase as aircraft age. Acquiring new aircraft is a means for lowering maintenance costs.<sup>96</sup> Newer aircraft also bring new advances in technology, which tend to lower operating costs. Boeing's new 787 model, for example, is the first aircraft to be made mostly of light-weight, composite materials, resulting in an estimated 20% lower fuel burn over similarly sized existing models.<sup>97</sup> An airline looking to maintain a competitive edge would prefer to acquire new aircraft, rather than operate a fleet of outdated, inefficient aircraft. Acquiring this new fleet requires a substantial amount of capital.

Before an airline can even be competitive, it needs to be sure it can stay afloat. The year 2008 was the start of trying times for the airline industry, characterized by a number of rapid collapses of airlines both new and old.<sup>98</sup> A common factor in all of their downfalls was an inability to maintain and acquire new capital when faced with the financial losses of the rough economic climate. The statements of airline officials and CEOs tell the story. "We had been clear, since closing on our last round of financing, that we would need additional capital. [I]nvestors believe in [Eos's] business model . . . [but] some issues arose that we could not overcome."<sup>99</sup> "[High oil prices and a struggling economy] have impeded [Champion Air's] efforts to attract new capital and new investors."<sup>100</sup> "[Aloha Airlines] said it ran out of time to find a qualified buyer or secure continued financing for its passenger

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<sup>94</sup> *Id.* at 29.

<sup>95</sup> Press Release, AirTran Airways, AirTran Airways Defers 18 Boeing Aircraft Deliveries (May 30, 2008), *available at* <http://pressroom.airtran.com/phoenix.zhtml?c=201565&p=irol-newsArticle&ID=1152174>.

<sup>96</sup> See JetBlue 2003 Annual Report, *supra* note 91, at 23 ("Because the average age of our aircraft is approximately 21 months, our aircraft require less maintenance now than they will in the future. . . . Our maintenance costs will increase significantly, both on an absolute basis and as a percentage of our operating expenses, as our fleet ages . . .").

<sup>97</sup> Matt Molnar, *Boeing 787 Dreamliner Finally Gets Off the Ground*, POPULAR MECHANICS, Dec. 15, 2009, <http://popularmechanics.com/technology/aviation/news/4339887>.

<sup>98</sup> See *supra* notes 1–5 and accompanying text.

<sup>99</sup> *Eos*, *supra* note 2.

<sup>100</sup> Walsh, *supra* note 3 (quoting Champion Air CEO Lee Steele).



business.”<sup>101</sup> “[ATA’s] top management began looking for other capital or, short of that, ways to sell the 35-year-old airline as a going concern, but could neither consummate a sale nor find other cash, forcing this morning’s shut down.”<sup>102</sup>

In sum, even the most efficient or innovative airlines require large amounts of capital. Without adequate access to this capital, the existing players cannot expand or improve their existing services, and new entrants do not have access to the market. In a worst-case scenario, airlines, even those with a strong capitalization, may not be able to sustain the losses brought about by an extended economic contraction. The end of cash signifies the end of an airline.

### *B. The Risks: Passenger Safety and Security*

Safety with regard to aircraft airworthiness and airline operations is one concern of foreign ownership. A noted risk is that foreign-owned airlines may not operate in accordance with the same standards of safety that airlines in the U.S. do.<sup>103</sup> Lelieur describes the concern about safety thusly: “[I]f a carrier is owned by nationals who are not citizens of the designating country, it may be difficult to demonstrate the designating government’s continuing competence in the technical aspects of airline and aircraft certification.”<sup>104</sup> Despite this possibility, concerns about safety can be adequately addressed through existing bilateral agreements and operating certification procedures.

If a foreign carrier did not meet international safety standards, the U.S. could revoke the carrier’s operating certificate in the U.S., thereby barring U.S.-bound flights on that particular carrier or all flights from the respective foreign country. More commonly, the Federal Aviation Administration (FAA) can impose restrictions on foreign carrier services to the U.S. based on concerns about safety. For example, in 2008 the FAA downgraded Israel’s safety ranking from Category I to Category II,<sup>105</sup> meaning that Israeli air carriers would be unable to expand existing service to the U.S. either through additional aircraft or flights.<sup>106</sup> The FAA scrutinized a number of factors, including lack of safety oversight and Israel’s crowded air space.<sup>107</sup> Korean Air suffered the same fate in the 1990s after a decades-long string of fatal crashes.<sup>108</sup> The category downgrade not only affected Korean Air, but it also affected Asiana Airlines, another international airline based in South Korea.<sup>109</sup> The fact that foreign airlines operating to the U.S. can be held to international safety standards suggests that U.S. carriers, even those owned

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<sup>101</sup> Segal, *supra* note 5.

<sup>102</sup> Jim Mathews, *ATA Airlines Shuts Down*, AVIATION WEEK, Apr. 3, 2008, [http://www.aviationweek.com/aw/generic/story\\_channel.jsp?channel=comm&id=news/ATA04038.xml](http://www.aviationweek.com/aw/generic/story_channel.jsp?channel=comm&id=news/ATA04038.xml).

by foreign entities, would be subject to the same standards as well. Additionally, the country in which an air carrier's aircraft are registered is recognized as responsible for aircraft airworthiness, which highlights the level of control the U.S. will maintain over its carriers, both U.S. and foreign owned.<sup>110</sup>

### C. *The Risks: A Loss of American Jobs*

A large constituency that has predominantly opposed the liberalization of foreign ownership restrictions has been airline employees.<sup>111</sup> When foreign

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<sup>103</sup> See, e.g., U.S. GOV'T. ACCOUNTABILITY OFFICE, OVERSIGHT OF FOREIGN CODE-SHARE SAFETY PROGRAM SHOULD BE STRENGTHENED 1 (2005) (analyzing the impact on aviation safety of international code-share agreements, citing concerns raised following the crash of a foreign airliner operating a code-share flight for a U.S. carrier).

<sup>104</sup> LELIEUR, *supra* note 24, at 64; see also Patel, *supra* note 10, at 520 (citing LELIEUR) ("Lelieur argues that because a clause exists in model bilateral agreements that allows a country to withdraw a carrier's operating permit if it fails to comply with international safety standards, aviation safety would not be endangered by further liberalization and relaxation of ownership restrictions.").

<sup>105</sup> Andy Pasztor, *IAA May Lower Isreal's Safety Rank*, WALL ST. J., Dec. 4, 2008, at D3, available at <http://online.wsj.com/article/SB122836333376578741.html>. These safety ratings are part of the International Aviation Safety Assessments Program created by the Federal Aviation Administration. *International Aviation Safety Assessments (IASA) Program*, FEDERAL AVIATION ADMINISTRATION, <http://www.faa.gov/about/initiatives/iasa/> (last visited Mar. 13, 2010). The program assess a foreign country's ability to adhere to internationally accepted safety standards. *Id.* For an overview of the two-category system, see *IASA Results Definitions*, FEDERAL AVIATION ADMINISTRATION, <http://www.faa.gov/about/initiatives/iasa/definitions/> (last visited Feb. 9, 2011).

<sup>106</sup> Zohar Blumenkrantz, *U.S. FAA Downgrades Israel's Aviation Safety Ranking*, HAARETZ, Nov. 20, 2008, <http://www.haaretz.com/hasen/spages/1038947.html>.

<sup>107</sup> *Id.*; see also Pasztor, *supra* note 105..3

<sup>108</sup> Don Kirk, *New Standards Mean Korean Air Is Coming off Many 'Shun' Lists*, N.Y. TIMES, Mar. 26, 2002, <http://www.nytimes.com/2002/03/26/business/new-standards-mean-korean-air-is-coming-off-many-shun-lists.html>.

<sup>109</sup> *Id.* The FAA most recently downgraded Mexico to Category 2, meaning that Mexican carriers could continue to operate or adjust frequencies on existing authorized services to the U.S., provided that the carriers' total capacity to the U.S. does not increase. Brendan Sobie, *Aeromexico Increases Capacity on Several U.S. Routes*, AIR TRANSPORT INTELLIGENCE NEWS, Oct. 27, 2010, <http://flightglobal.com/articles/2010/10/27/349020/aeromexico-increases-capacity-on-several-us-routes.html>.

<sup>110</sup> LELIEUR, *supra* note 24, at 64.

<sup>111</sup> See, e.g., Letter from Edward Wytkind, President, AFL-CIO Transp. Trades Dep't (TTD), to Don Young, Chairman, House Transp. & Infrastructure Comm., and James Oberstar, Ranking Democrat, House Transp. and Infrastructure Comm. (Nov. 2,

investors or air carriers purchase U.S. airlines, the fear is that they will begin to replace American employees with foreign ones.<sup>112</sup> A related fear is that a foreign carrier may purchase a U.S. carrier to gain access to the latter's U.S. domestic network in an effort to feed passengers to the foreign carrier's international routes from the U.S.<sup>113</sup> In such a scenario, the foreign carrier would likely discontinue the U.S. carrier's international routes so that it could operate the routes itself. U.S. employees would be shut out of more highly salaried international service positions.<sup>114</sup> Indeed, the British Airways-US Air deal did seem to limit US Air's international services to two cities—Paris and Frankfurt<sup>115</sup>—but after the conclusion of the agreement US Air aggressively expanded its international operations from its Philadelphia hub.<sup>116</sup>

Proponents of liberalization often counter that, during times of intense economic distress and significant layoffs in the airline industry, foreign investment would provide a needed lifeline to sustain the airlines and curb the job losses.<sup>117</sup> Other proponents argue that U.S. airlines in close arrangements with foreign carriers would be unlikely to cut their international services because such services are usually the most lucrative of their route networks.<sup>118</sup> While profits on domestic operations for U.S. carriers are squeezed by the presence of low-fare carriers, international operations have been a haven for the legacy carriers to operate free of most low-fare competition.<sup>119</sup>

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2005), available at [http://www.ttd.org/index.asp?Type=B\\_PR&SEC={2E972A88-C3BB-43B7-9D07-52BDEA6D8C0E}](http://www.ttd.org/index.asp?Type=B_PR&SEC={2E972A88-C3BB-43B7-9D07-52BDEA6D8C0E}) (follow "Oppose Changing Statutory Rules Limiting Foreign Ownership of U.S. Airlines: Letter to the House" hyperlink) (voicing opposition on behalf of the AFL-CIO TTD to the Bush Administration's proposal to liberalize ownership restrictions in airlines).

<sup>112</sup> LELIEUR, *supra* note 24, at 65.

<sup>113</sup> Patel, *supra* note 10, at 514.

<sup>114</sup> *Id.*

<sup>115</sup> See *USAir Route System*, USAIR MAGAZINE, May 1996, at 94, 94–95. The May 1996 issue of USAir Magazine also included a global route map for its partner British Airways. *Id.* at 96–97.

<sup>116</sup> See *US Airways Route System*, US AIRWAYS, April 1997, at 94, 94–95. The April 1997 issue of US Airways' magazine did not include a British Airways route map as the May 1996 issue did. Within the one year period since May 1996, US Air ended its agreement with British Airways, changed its name to US Airways, and added three cities to its transatlantic network: Munich, Rome, and Madrid. *Id.*

<sup>117</sup> LELIEUR, *supra* note 24, at 66.

<sup>118</sup> See Patel, *supra* note 10, at 514.

<sup>119</sup> David Bond, *Stymied by Domestic Fares, U.S. Carriers Think International*, AVIATION WEEK, Oct. 9, 2005, [http://www.aviationweek.com/aw/generic/story\\_generic.jsp?channel=awst&id=news/10105p01.xml](http://www.aviationweek.com/aw/generic/story_generic.jsp?channel=awst&id=news/10105p01.xml).

To some extent, the arguments on both sides of the issue are valid. Airlines will likely cut jobs or stymie job growth on international routes if foreign carriers invest in U.S. carriers. On the other hand, international routes are many legacy airlines' bread and butter. Nevertheless, the fact of the matter is airlines will, and have, cut services and jobs on their international sectors already without any relaxation of foreign ownership restrictions, and they have done so through code-share agreements with foreign carriers.<sup>120</sup> Instead of operating an international route, a U.S. airline can put its code on a foreign carrier's flight, thereby profiting off an international flight that the U.S. airline does not operate.<sup>121</sup>

With the existence of the current U.S.-EU Open Skies agreement and international airline alliances across the Atlantic, increased transatlantic competition may have slightly diminished the profitability of these routes, making a code-share arrangement or low-risk joint venture more appealing. While some scholars have noted that U.S. airlines would not give up their international routes,<sup>122</sup> some airlines have found ways to profit off of international routes without expending most of the cost of operating such routes. United Airlines recently took advantage of Open Skies to contract with Aer Lingus, the flag carrier of Ireland, to operate flights from United's hub in Washington Dulles International Airport to Barajas Airport in Madrid.<sup>123</sup> Flights began operating with Aer Lingus equipment and cockpit crew in March 2010.<sup>124</sup> United Airlines employees were, at the very least,

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<sup>120</sup> LELIEUR, *supra* note 24, at 19 ("[C]arriers most frequently cooperate through 'code-sharing,' whereby airlines place their code on the flights of another carrier, sell the service as their own.").

<sup>121</sup> *Id.*

<sup>122</sup> See Patel, *supra* note 10, at 515 ("[T]here are essentially two ways in which international service could be contracted: (1) if a foreign-owned company starts up a U.S. subsidiary or buys a U.S. carrier; and (2) if a code-sharing partner, such as Lufthansa, replaces a U.S. carrier such as United, on long haul routes. . . . With respect to the second possibility of code sharing and transferring international routes to the foreign carrier (such as the case where United and Lufthansa would agree that Lufthansa would operate all long haul services), international service is simply too profitable to logically see a domestic U.S. carrier willing to cede its long haul operations to a foreign code sharing partner.").

<sup>123</sup> Press Release, United Airlines Press Office, Aer Lingus and United Airlines Announce Transatlantic Partnership (Jan. 22, 2009) *available at* <http://www.united.com/press/detail/0,7056,60202-1,00.html>.

<sup>124</sup> *Id.* While the cockpit would be staffed by Aer Lingus pilots, a third party contractor hired cabin crew specifically for the new route. Julie Johnsson, *United Airlines Unions Protest Aer Lingus Venture*, CHI. TRIB., Mar. 18, 2010, at 1.

irritated by this agreement, as they believed the route could be operated with United's own aircraft and employees.<sup>125</sup>

Even prior to the United-Aer Lingus agreement, Northwest and KLM—and now Delta,<sup>126</sup> KLM, and Air France—have jointly operated flights between European hubs and cities in the U.S., alternating equipment and crew as the airlines have seen fit. Generally the switches are made to take advantage of an aircraft type that is better suited to a particular route, but a type that is only available to one airline in the partnership and not the other. For example, Air France used to operate wide-bodied, higher capacity aircraft into Philadelphia International Airport from its hub at Paris Charles De Gaulle International Airport. Due to decreasing demand requiring a decrease in aircraft size, Delta took over the route using its narrow-bodied Boeing 757s, an aircraft type that Air France does not operate.<sup>127</sup> In this scenario, the American airline employee gains a flight; however, there are plenty of potential scenarios in which the same employee could lose work as well. Delta, for example, could operate a route with a Boeing 747, the largest in its fleet, to a slot-restricted airport,<sup>128</sup> and when the demands on the route exceed the capacity of the aircraft, Air France may have to take over the flight with its higher capacity Airbus A380s, an aircraft which neither Delta nor any U.S. carrier operates.

In some sense, the damage that airline employees fear from liberalization of the foreign ownership restrictions has already taken place with Open Skies

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<sup>125</sup> *United Airlines Seems Determined to Piss off Employees; O'Leary Tees Off on News*, PLANEBUZZ, (Jan. 23, 2009, 12:46 PM), [http://www.planebuzz.com/2009/01/united\\_airlines\\_seems\\_determin.html](http://www.planebuzz.com/2009/01/united_airlines_seems_determin.html).

<sup>126</sup> Delta Air Lines recently acquired Northwest Airlines and now operates under one operating certificate. Marilyn Adams and Dan Reed, *World's Largest Airline: Delta, Northwest in Merger Deal*, USA TODAY, Apr. 14, 2008, [http://www.usatoday.com/travel/flights/2008-04-14-delta-northwest-merge\\_N.htm](http://www.usatoday.com/travel/flights/2008-04-14-delta-northwest-merge_N.htm).

<sup>127</sup> Press Release, Air France, Air France KLM 2009 Winter Schedule (Sept. 21, 2009), <http://corporate.airfrance.com/en/press/press-releases/> (browse through the pages until press releases for "Monday 21 September 2009" are displayed; then follow "Air France KLM 2009 Winter Schedule" hyperlink under the September 21 date). Air France does not deploy aircraft with capacity and operational characteristics similar to those of the Boeing 757 on transatlantic (long-haul) routes. See *Key Figures*, AIR FRANCE, <http://corporate.airfrance.com/en/fleet/long-haul-fleet/key-figures/> (last visited Mar. 25, 2011).

<sup>128</sup> Airports are often slot-restricted when heavy congestion in aircraft movements outstrips the capacity of the airport's limited number of runways. See Michael E. Levine, *Airport Congestion: When Theory Meets Reality*, 26 YALE J. ON REG. 37, 43–44 (2009) (discussing airport congestion at airports with significant operations by more than one carrier and the need for slots or congestion pricing). Because airlines do not have the flexibility to increase the number of flights at such airports, they are forced to expand capacity through larger aircraft.

and global airline alliances. Allowing foreign investment in U.S. carriers would seem to do no more harm than has already been done, from the point of view of the airline employee.

#### *D. The Risks: Inadequate Aircraft for National Defense*

##### *1. Civil Reserve Air Fleet Program*

With regard to national security, the primary concern for not loosening the investment restrictions has traditionally been the preservation of the Civil Reserve Air Fleet (CRAF) program, coordinated by the Department of Defense (DOD). In CRAF, U.S. airlines are incentivized to transport U.S. personnel and cargo overseas on behalf of the U.S. government during times of war.<sup>129</sup> By some accounts, airline participation accounts for up to half of the U.S. military's airlift capability during wartime, while the military saves cost on purchasing, maintaining, and staffing additional military aircraft throughout peacetime.<sup>130</sup> The incentives to airlines are multifold. For one, airlines have traditionally experienced lower passenger numbers during wartime, and the excess aircraft capacity available to them is better utilized while under the service of the U.S. government.<sup>131</sup> The second benefit is that airlines that choose to participate in the program are offered the opportunity to support the military's charter needs during peacetime, another potentially lucrative deal for the participating U.S. airlines.<sup>132</sup> For the most part airlines participate in this program because it simply makes good business sense.

Currently CRAF requires participants to be U.S. carriers certified by the FAA.<sup>133</sup> As of 2007, membership included 37 carriers and over 1,300

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<sup>129</sup> Patel, *supra* note 10, at 520.

<sup>130</sup> CHRISTOPHER BOLKCOM, CONG. RESEARCH SERV., NO. RL33692, CIVIL RESERVE AIR FLEET (CRAF) 4 (2006).

<sup>131</sup> See, e.g., INDUSTRIAL COLLEGE OF THE ARMED FORCES, INDUSTRY STUDIES 2002: TRANSPORTATION 19 (2002), available at <http://www.dtic.mil/cgi-bin/GetTRDoc?AD=ADA425298&Location=U2&doc=GetTRDoc.pdf> (noting how the September 11th attacks resulted in excess aircraft capacity for U.S. airlines, capacity which went toward military uses in Afghanistan).

<sup>132</sup> GAO 1992, *supra* note 14, at 15; see also INSTITUTE FOR DEFENSE ANALYSES, ECLAT CONSULTING, GRA, MORTEN, BEYER & AGNEW, SUSTAINING THE CIVIL AIR RESERVE FLEET (CRAF) PROGRAM 1 (2003) [hereinafter IDA CRAF Study], available at [http://www.acq.osd.mil/log/tp/new\\_airlift\\_policies/craf\\_study\\_final\\_%20may12003.pdf](http://www.acq.osd.mil/log/tp/new_airlift_policies/craf_study_final_%20may12003.pdf) (finding the peacetime military charter business to total \$2 billion annually during the early 2000s).

<sup>133</sup> BOLKCOM, *supra* note 130, at 1.

aircraft.<sup>134</sup> Based on the varying capabilities of their aircraft, CRAF carriers are enlisted on any of three main mission segments: the international segment (long and short range), the national segment (sections for the continental U.S. and Alaska), and aeromedical evacuation.<sup>135</sup> Out of these segments, carriers provide the most support by far for CRAF's international operations,<sup>136</sup> suggesting that DOD's wartime operations abroad would be the most impacted should CRAF participation diminish. To date, CRAF has only been activated formally twice in its 54-year history: once during Operation Desert Shield/Storm in 1990–91, and once during Operation Iraqi Freedom in the first half of 2003.<sup>137</sup> In both instances, the government activated CRAF's long range international operations, though cargo was not required for Iraqi Freedom.<sup>138</sup>

Opponents of liberalizing foreign ownership restrictions argue that the government will have fewer options in ensuring that CRAF has adequate support for its wartime initiatives, once foreign companies gain control of U.S. airlines.<sup>139</sup> U.S. airlines presently have a strong financial incentive not only to participate in CRAF, but also to fulfill their CRAF obligations if the program were to be activated.<sup>140</sup> As a result, the concern over foreign ownership does not rest solely on whether a foreign-controlled airline will participate in CRAF, but whether the airline will come through on its obligations. With U.S. airlines, the government has the power to threaten to revoke an airline's operating certificate (causing it to cease operations altogether) or threaten litigation upon company officers and directors, if noncompliance causes CRAF participation to fall below military requirements.<sup>141</sup> Foreign-owned airlines, particularly those controlled by

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<sup>134</sup> *Factsheets: Civil Air Reserve Fleet*, UNITED STATES AIR FORCE, <http://www.af.mil/information/factsheets/factsheet.asp?id=173> (last visited Feb. 5, 2010) [hereinafter USAF CRAF Factsheet]. In 2006, all major passenger and cargo carriers participated in CRAF, suggesting the carriers financially benefited from the program. BOLKCOM, *supra* note 130, at 8. At the time, the major passenger carriers were United, American, Delta, Northwest, US Airways, and Southwest Airlines, and the major cargo carriers were UPS and FEDEX. *Id.* at 8 n.17.

<sup>135</sup> *Id.* at 1.

<sup>136</sup> USAF CRAF Factsheet, *supra* note 134.

<sup>137</sup> BOLKCOM, *supra* note 130, at 3.

<sup>138</sup> *Id.*

<sup>139</sup> See Patel, *supra* note 10, at 521 (noting that the U.S. government has less leverage over foreign carriers should one fail to fulfill CRAF obligations). But see INDUSTRIAL COLLEGE OF THE ARMED FORCES, *supra* note 131, at 17–19 (suggesting that DOD should supplement existing airlift needs using foreign carriers, particularly those allied with U.S. carriers).

<sup>140</sup> IDA CRAF Study, *supra* note 132, at 39.

<sup>141</sup> Patel, *supra* note 10, at 521.

foreign governments, could be at odds with U.S. foreign policy, and if they exerted control over U.S. carriers necessary for the success of CRAF, they could frustrate the U.S. government's military objectives abroad, even when non-participation in CRAF were financially damaging to the airline. For this reason, both proponents and opponents of liberalization have voiced a need for the U.S. government to exert sizeable influence over airlines controlled by foreign or domestic entities.<sup>142</sup>

## 2. *Dangers of Foreign Government Control and Interference*

The CRAF program is most vulnerable if foreign government-controlled entities, or foreign governments themselves, purchase U.S. airlines. Prior to the 1990s, government ownership and control of national airlines was the norm in the international aviation environment.<sup>143</sup> Foreign governments, compelled by concerns of nationalism and competition from the air carriers of other countries, sought to maintain control of national airlines to sustain them and promote national economic goals.<sup>144</sup> As the international airline industry matured, state-ownership of flag carriers began to wane in popularity, giving way to the industry's liberalization as a whole—complete with healthy competition by privately-owned airlines.<sup>145</sup> The result of widespread privatizations has been an industry where many national flag carriers are partially owned, but not controlled, by their home governments.<sup>146</sup> Nevertheless, many countries, both economically developed and lesser developed, still hold controlling interests in their home carriers to this day for various reasons.<sup>147</sup>

The state control of these foreign airlines raises questions about the possibility that, should foreign ownership restrictions in U.S. airlines loosen, foreign governments could have influence over whether a U.S. airline participates in CRAF. The distinctions between private and public

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<sup>142</sup> See, e.g., Patel, *supra* note 10, at 521–22.

<sup>143</sup> LELIEUR, *supra* note 24, at 3.

<sup>144</sup> See ZYLICZ, *supra* note 62, at 23 (“The usual attitude of states that have small or medium size airlines which are not strong enough to stand the competition from foreign, more powerful companies, is to protect their national airlines through various modes of regulation and restriction . . . rather than to expose them to risk of possible failure.”). This same rationale can be used to explain the traditional desire for many countries with vulnerable national airlines to control a nation's flag carrier and protect it from failure.

<sup>145</sup> LELIEUR, *supra* note 24, at 75.

<sup>146</sup> *Id.*

<sup>147</sup> See discussion *infra* Part IV.A.3.



corporations<sup>148</sup>—that is, state-owned and state-controlled corporations—strike at the core of this issue. Both private and public corporations have differing constituent groups to whom they must answer.<sup>149</sup> Private corporations answer to shareholders while public corporations often answer to a government’s electorate.<sup>150</sup>

Shareholders of private corporations have a primary interest in maximizing the long term value of their shares, an interest which demands strong corporate profits. In other words, a corporation “must have the making of money as its primary goal. If it fails to thrive financially, the private corporation faces ruin.”<sup>151</sup> Managers of private corporations are first and foremost answerable to their shareholders,<sup>152</sup> which places a burden on the managers to make corporate decisions that will profit the corporation. In the context of U.S. airline ownership, foreign airlines owned by private investors are far more likely to voluntarily participate in CRAF than are those run by governments because participation results in profit. If a foreign airline gained control of a U.S. airline, the financial benefits of participation in CRAF would likely outweigh any potential downside.<sup>153</sup>

An independent-minded manager could decide not to participate in CRAF, but she would face potential removal from office if shareholders strongly disapproved of the decision. Along a similar line, independent-minded *investors* may choose not to allow their airline to participate in CRAF against any reasonable business judgment.<sup>154</sup> Such independent-minded investors would not be unique to foreign countries, however. U.S. investors could still impose the same poor business decisions on an airline for their own personal reasons. It is not unreasonable to imagine a wealthy American mogul vocally opposing U.S. military intervention while in control

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<sup>148</sup> In the context of this Note, “public” refers to a corporation that is state-owned or state-controlled. This is distinguishable from a publicly traded company that is private in nature but owned by investors trading on a public exchange.

<sup>149</sup> Shirley L. Mays, *Privatization of Municipal Services: A Contagion in the Body Politic*, 34 DUQ. L. REV. 41, 59 (1995).

<sup>150</sup> *Id.* at 59 n.115.

<sup>151</sup> *Id.* at 59.

<sup>152</sup> Rutheford B. Campbell, Jr. and Christopher W. Frost, *Managers’ Fiduciary Duties in Financially Distressed Corporations: Chaos in Delaware (and Elsewhere)*, 32 J. CORP. L. 491, 495–97 (2007).

<sup>153</sup> See *supra* notes 129, 131–33 and accompanying text for a discussion on why airlines naturally benefit from participation in CRAF.

<sup>154</sup> See Patel, *supra* note 10, at 522 (noting the possibility that a foreign investor could choose not to participate in CRAF for independent reasons).

of a U.S. airline. Ted Turner, for example, has voiced his distaste for war,<sup>155</sup> and it would be possible that an airline in his hands would not participate in CRAF. In the end, the threat that an investor would prevent a U.S. airline from participating in CRAF exists regardless of the nationality of the investor. Despite this fact, private investment from foreign or domestic sources will still tend to favor participation in CRAF.

Public corporations, on the other hand, have responsibilities that “go beyond the desire for monetary gain.”<sup>156</sup> The managers of public corporations are often held accountable to the government, which in turn is accountable to the electorate. If a public corporation does not align its actions with the will of the general public, the government owners may suffer politically. For this reason, the governments of democratic countries have the potential to be influenced by political considerations when exerting control over public corporations.<sup>157</sup> A state-owned foreign airline would pose risks to CRAF that a privately held airline would not. The foreign government owning the foreign airline may feel pressured by its electorate into not aiding the U.S. in its wartime efforts. Public opposition to a U.S.-led war could influence a foreign government to ensure that a U.S. airline it indirectly controls will refuse to participate in the CRAF program.

On top of political considerations, foreign governments are fundamentally responsible for protecting their nations’ security interests. In the unlikely scenario that the U.S. government were to go to war with a foreign country whose government exerts control over a U.S. airline, or with an ally thereof, the purposes of CRAF would again be undermined. In the past, an extreme scenario such as this would have likely been cause for the U.S. government to seize the U.S.-registered aircraft indirectly controlled by foreign carriers through the Defense Production Act.<sup>158</sup> Today, a possible safeguard against this remote scenario would come from the Committee on Foreign Investment in the United States (CFIUS), which authorizes the Executive Branch to approve or investigate the national security implications of a pending transaction involving a foreign investor.<sup>159</sup> Additionally, as an

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<sup>155</sup> Interview by Jesse Kornbluth, Reader’s Digest, with Ted Turner (Nov. 21, 2008), in *READER’S DIGEST*, Dec. 2008, at 27 (“War with Iran wouldn’t be fun. War with Russia would be catastrophic. War is no longer any kind of answer.”).

<sup>156</sup> Mays, *supra* note 149, at 60.

<sup>157</sup> See *id.* (discussing how municipal corporations have political responsibilities).

<sup>158</sup> Patel, *supra* note 10, at 521 (discussing the Defense Production Act of 1950, Pub.L. No. 81-774, § 201, 64 Stat. 799–800 (1950) (codified under 50 U.S.C. app. § 2061 *et seq.* (2006) and repealed Sept. 30, 2009)). The Act authorized the President to condemn property to aid national defense. 50 U.S.C. app. § 2081 (2006), *repealed by* the Defense Production Act Reauthorization of 2009, Pub.L. No. 111-67, § 2(a)(2), 123 Stat. 2006, 2007 (Sept. 30, 2009).

<sup>159</sup> 50 U.S.C. app. § 2170 (2006).

enforcement mechanism for any carrier that volunteers to participate in CRAF but wavers in meeting its commitments, DOT could revoke a carrier's operating certificate.<sup>160</sup> Requiring CRAF participation before any certification is granted, however, poses a potential downside: the requirement could, in effect, deter foreign investors from investing in U.S. carriers from the outset, which would likely undo the benefits of liberalizing ownership restrictions. Many also believe that such a requirement would be unduly restrictive on airlines, particularly when free market principles encourage maximum free choice in commercial decisions.<sup>161</sup>

In 2005, DOT proposed a rule to partially liberalize foreign ownership restrictions while guarding against the national security risks of foreign involvement in CRAF.<sup>162</sup> In particular, DOT proposed that its interpretation of "actual control" by U.S. citizens should be narrowed to those aspects of an airline's operations that affect national security concerns and participation in CRAF.<sup>163</sup> Essentially, foreign investors would have more freedom to control the purely commercial aspects of an airline's operations, but the airline would have to designate U.S. citizens to carry out its decisions with regard to CRAF participation. This arrangement could have proven problematic, since, for example, it did not seem realistic to expect a subordinate committee of U.S. citizens to be fully independent of a foreign-controlled airline board. With multiple parties expressing views on both sides of the proposed rule, DOT withdrew its proposal, citing its "controversial" nature as a reason to delay any rulemaking until further public discussion on the issue could take place.<sup>164</sup>

Apart from the national security implications, another potential problem involving government interference is the fact that foreign governments often subsidize the operations of their nation's carriers, whether as a response to government ownership of the carrier or as a means of saving a national airline during a time of crisis. Government subsidies often have a damaging effect on both airlines themselves and on competition generally. On the one hand, airlines which are supported by their governments may operate

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<sup>160</sup> Josh Cavinato, Note, *Turbulence in the Airline Industry: Rethinking America's Foreign Ownership Restrictions*, 81 S. CAL. L. REV. 311, 331 (2008).

<sup>161</sup> See, e.g., Patel, *supra* note 10, at 522.

<sup>162</sup> Actual Control of U.S. Air Carriers, 70 Fed. Reg. 67,389, 67,393 (proposed Nov. 7, 2005).

<sup>163</sup> *Id.* at 67,394. The proposed rule restricted the possibility of increased foreign investment to countries that had Open Skies agreements with the U.S. and with which the U.S. had reciprocal investment benefits. *Id.*

<sup>164</sup> Actual Control of U.S. Air Carriers, 71 Fed. Reg. 71,106, 71,108–09 (Dec. 8, 2006).

inefficiently due to a lack of incentive to operate profitably.<sup>165</sup> The result is lower productivity accompanied by higher operating costs, which have a detrimental effect on the consumer by way of higher prices.<sup>166</sup>

On the other hand, airlines may be able to unfairly use their government subsidies to undercut competition from foreign carriers.<sup>167</sup> In one possible scenario, an airline that is not concerned about profitability theoretically could be able to charge any fare it wants, no matter how low. This would disadvantage carriers who could not afford to charge fares as low, and they would be driven out of the market. As it relates to foreign ownership in U.S. airlines, a foreign government that subsidizes its national airline would, in effect, be subsidizing the U.S. airline that the foreign airline controls. If that U.S. airline no longer felt the pressure to charge a profitable fare, it would unfairly harm the domestic business of other U.S. airlines that were not controlled by a foreign entity.<sup>168</sup> The market would tilt in favor of foreign-owned U.S. airlines subsidized by foreign governments.

Governments in both the United States and abroad have succumbed to pressure to subsidize national carriers at various times in the recent past. For example, though barred by the Maastricht Treaty from aiding their carriers,<sup>169</sup> EU governments during the 1990s supported their home nation carriers in Spain, France, and Greece.<sup>170</sup> This aid essentially constituted bail-out packages to keep ailing national airlines from failing.<sup>171</sup> The U.S. government subsidized one of its own carriers following the September 11,

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<sup>165</sup> Jason S. Kelley, *Privatization of Transportation in Developed Nations*, 48 ADMIN. L. REV. 545, 551 (1996).

<sup>166</sup> *Id.*

<sup>167</sup> LELIEUR, *supra* note 24, at 75 (“[T]he airlines, constantly provided with government subsidies, may be more tempted to offer lower prices to consumers than private carriers would be, and, consequently, they would dominate the market.”).

<sup>168</sup> See Kirsten Böhmman, *The Ownership and Control Requirement in U.S. and European Union Air Law and U.S. Maritime Law—Policy; Consideration; Comparison*, 66 J. AIR L. & COM. 689, 697 (2001) (“The statutory requirement of U.S. citizenship was intended to prevent a [heavily subsidized,] state-owned carrier from buying a U.S. carrier and competing unfairly in the U.S. domestic market to the detriment of other U.S. carriers.”).

<sup>169</sup> The current iteration of the treaty exists as Treaty on European Union and Treaty on the Functioning of the European Union, Sept. 5, 2008, 2008 O.J. (C 115) 1. “[A]ny aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market.” *Id.* art. 107(1).

<sup>170</sup> Kelley, *supra* note 165, at 553. Specifically, the Spanish government gave Iberia Airlines a \$945 million aid package in 1992; France gave Air France a \$3.8 billion aid package in 1994; Greece gave Olympic Airlines a \$2.3 billion aid package in 1994. *Id.*

<sup>171</sup> *Id.*

2001 attacks, bailing out America West Airlines in December 2001.<sup>172</sup> The government's Air Transportation Stabilization Board accepted a request to guarantee loans of nearly \$380 million to America West Airlines, receiving warrants representing 5.3% of the airline's common stock, although the government would not be entitled to voting rights.<sup>173</sup>

Despite the general trend toward privatization, the risk of some foreign airlines becoming public or nationalized still exists, though it does appear somewhat remote. Countries that are concerned about the state of their home carriers, for example, may be tempted to take ownership or control of their struggling carriers to prevent the collapse of the airline's operations. As stated above, the U.S. government invested heavily in America West Airlines after the September 11th attacks to prevent the airline's collapse.<sup>174</sup> In the case of Bahrain's Gulf Air, the state's sovereign wealth fund, Mumtalakat, ceded direct control of Gulf Air to the state because of the airline's perceived lower rate of return.<sup>175</sup> Another possibility exists that a leader of government, for ideological or political reasons, might nationalize private assets, including the national airlines.

#### IV. A CAUTIOUS SOLUTION: LIBERALIZING RESTRICTIONS WITH CONTINUED VIGILANCE

Among scholarly opinion, liberalization of foreign investment restrictions is the commonly accepted policy goal, particularly in the wake of a turbulent decade in the airline industry.<sup>176</sup> Having dispelled many

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<sup>172</sup> U.S. GEN. ACCOUNTING OFFICE, COMMERCIAL AVIATION: FINANCIAL CONDITION AND INDUSTRY RESPONSES AFFECT COMPETITION 5 n.8 (2002), available at <http://www.gao.gov/new.items/d03171t.pdf> ("The Board approved a loan of \$429 million to America West Airlines.").

<sup>173</sup> Letter from Roger Kodat, Acting Executive Dir., Air Transp. Stabilization Bd., to W. Douglas Parker, Chairman, President, Chief Executive Officer, Am. W. Airlines (Dec. 28, 2001) (on file with author). America West Airlines acquired US Airways (and adopted its name) in September 2005, retaining W. Douglas Parker as CEO of the new US Airways. See US AIRWAYS GROUP, INC., 2005 ANNUAL REPORT 7 (2005).

<sup>174</sup> See *supra* notes 172–73 and accompanying text.

<sup>175</sup> Frederik Richter, *Bahrain SWF Moves Gulf Air Ownership to Govt*, REUTERS (Feb. 4, 2010), <http://www.reuters.com/article/idUSLDE6132TC20100204>. Note, however, that this situation involved a carrier that was already *indirectly* controlled by the state; Gulf Air simply became *directly* controlled by the state after this divestiture. Actual privatization was still on the table. *Id.*

<sup>176</sup> See, e.g., LELIEUR, *supra* note 24, at 17; Patel, *supra* note 10, at 488; see also Carlos Grau Tanner, *New Proposals to Break the Foreign Ownership Deadlock in the Airline Industry*, 34 AIR & SPACE L. (vol. 2) 127, 127–34 (2009); Christopher McBay, Note, *Airline Deregulation Deserves Another Shot: How Foreign Investment Restrictions*

arguments against the removal of those restrictions, the issue of national defense and CRAF still remains on the table. Tearing down the wall of foreign ownership restrictions in one swoop could potentially prove onerous to CRAF, for example, if there is no continued oversight of changes in U.S. airline ownership.<sup>177</sup> For this reason, this Note argues that liberalization should first be specifically tailored to EU nations, and that DOT should continue to review U.S. airlines for ownership and control requirements, particularly when a change in ownership places airline control in the hands of foreign entities from countries not signatories to any Open Skies agreement with the U.S., or when the foreign entity is controlled by a foreign government.<sup>178</sup>

#### *A. Foreign Investment Restrictions Should Be Relaxed to EU Entities*

The U.S.'s Open Skies agreement with the EU presents a unique opportunity for the U.S. to loosen its foreign investment restrictions. Although there remain several challenges with regard to government interference and control in particular EU member states, allowing EU entities to provide capital to U.S. airlines in exchange for some increased control is potentially the safest and most beneficial way for U.S. airlines to raise capital from foreign sources while addressing concerns about national defense and CRAF participation.

First, the Open Skies agreement between the U.S. and EU allows U.S. carriers to commercially operate any route between the U.S. and Europe, as well as intra-European routes,<sup>179</sup> a benefit whose magnitude is unmatched by other Open Skies agreements. This benefit was under threat prior to the second stage agreement in June 2010; relaxation of U.S. foreign ownership restrictions was a key issue for resolution during second stage talks, though no significant changes resulted.<sup>180</sup> Second, the U.S. and EU agreement includes a clear commitment of minimizing government interference and subsidies in the respective airlines of both communities. Such aspirational language exists in nearly all Open Skies agreements that the U.S. has

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*and Subsidies Actually Hurt the Airline Industry*, 72 J. AIR L. & COM. 173, 173–74 (2007).

<sup>177</sup> See, e.g., Cavinato, *supra* note 160, at 337 (“In order to address national security concerns, such as protecting the viability of the CRAF, the law should not lift the restriction entirely, but rather should incorporate certain conditions on foreign ownership and control.”).

<sup>178</sup> See IDA CRAF Study, *supra* note 132, at 47–50 (proposing that DOD assess the national security implications of any change in U.S. airline ownership).

<sup>179</sup> See *supra* note 78 and accompanying text.

<sup>180</sup> See *infra* notes 182–87 and accompanying text.

signed.<sup>181</sup> The U.S.-EU agreement, however, not only provides more direct language on the issue of subsidies, but the airline industry in the EU has shown more steady progress toward airline privatization than in most parts of the globe.<sup>182</sup> Third, nationalism in EU airlines is not as dominant a force as it once was with regard to airline ownership in the EU. Various EU airlines are no longer owned by citizens of their respective member states, but rather by airlines from other EU member states besides their own.<sup>183</sup> As EU members become more comfortable with these arrangements and less protective of their national carriers, the likelihood of government intervention decreases. And fourth, most EU states are also members of the North Atlantic Treaty Organization (NATO), a mutual defense pact. Foreign airlines based in NATO countries are less likely to subvert participation in CRAF, even if they are controlled by their home governments.

### 1. *The Specific Benefits of the U.S.-EU Open Skies Agreement*

The U.S.'s treatment of foreign investment restrictions has the potential to impact the continued success of the U.S.-EU Open Skies liberalization process. The 2007 agreement required "second stage negotiations" centered on a handful of priorities, one of the more contentious being the issue of "additional foreign investment opportunities."<sup>184</sup> Prior to the signing of the second stage agreement, the parties had a right to suspend all of the rights provided in the agreement if the second stage negotiations failed by a particular date.<sup>185</sup> The second stage provision was a requirement inserted by EU negotiators, to whom it was apparent that the initial Open Skies deal favored U.S. interests over EU interests.<sup>186</sup> For example, U.S. airlines were given the right to fly commercially between two points in different EU member states while EU airlines could not do the same between two U.S. states, nor could EU carriers sufficiently invest in U.S. airlines to acquire the same rights.<sup>187</sup> Additionally, the agreement opened up London's Heathrow

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<sup>181</sup> See *infra* text accompanying notes 200–03.

<sup>182</sup> See *infra* Part IV.A.2.

<sup>183</sup> See *infra* notes 217–22 and accompanying text.

<sup>184</sup> U.S.-EU Agreement, *supra* note 77, art. 21(2)(b).

<sup>185</sup> *Id.* art. 21(3).

<sup>186</sup> See *The Aeropolitics of the Oneworld Order*, AVIATION LAW PROF BLOG (Feb. 15, 2010), <http://lawprofessors.typepad.com/aviation/2010/02/the-aeropolitics-of-the-oneworld-order.html> [hereinafter *Aeropolitics*]; see also ASS'N OF EUROPEAN AIRLINES, OPEN SKIES: THE EU-US AIR TRANSPORT AGREEMENT 2–3 (Apr. 2, 2008), available at <http://files.acea.be/News/News020408.pdf> (listing the agreement's imbalances favoring U.S. airlines).

<sup>187</sup> See *supra* notes 78–80 and accompanying text.

Airport to all U.S. carriers, a right the United Kingdom seemingly gave up without increased investment rights in return.<sup>188</sup>

The second stage agreement eliminated a timetable for continued talks,<sup>189</sup> allowing the issue of foreign investment restrictions to fade into the background. Although the agreement no longer mandates discussion regarding investment restrictions, the overall agreement still operates on a provisional basis.<sup>190</sup> Other Open Skies agreements vest in parties the right to terminate the agreement at any time.<sup>191</sup>

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<sup>188</sup> *Aeropolitics*, *supra* note 186. Access to Heathrow prior to the agreement was limited to two U.S. carriers. *See supra* note 68 and accompanying text.

<sup>189</sup> U.S.-EU Amended Agreement, *supra* note 82, art. 6 (deleting the original agreement's Article 21, which provided for second stage talks and the right to suspend the agreement). Instead the amendment replaces second stage talks with "Further Expansion of Opportunities," where, if the parties meet certain conditions, each side can receive some additional traffic rights. *Id.* These rights involve seventh freedom rights—in the U.S.'s case, the right to operate a standalone flight between the EU and any of five non-EU countries without requiring the flight to originate or terminate in the U.S. *Id.* art. 6 (amended art. 21(3)(b)). The rights may likely prove useless for two reasons: first, the rights are conditioned upon the U.S. allowing EU entities to take ownership or control of U.S. airlines, a right that is reciprocated by the EU allowing U.S. investors to take control of EU airlines. *Id.* art. 6 (amended art. 21(2)). If that were to occur, U.S. airlines would likely prefer to invest in an EU airline to gain access to EU-third party routes, rather than operating the routes themselves and being subject to the limitations of the amended agreement. Second, seventh freedom access to a third party may require additional negotiation in the future, since current bilateral agreements tend to restrict the negotiated access benefits to airlines controlled by parties to the bilateral agreement—so-called "nationality clauses." *See The Nationality Clause Lives*, AVIATION LAW PROF BLOG (Mar. 2, 2010), <http://lawprofessors.typepad.com/aviation/2010/03/the-nationality-clause-lives.html>. As such, a U.S. airline could not operate a route from London to Cairo, for example, if the EU-Egypt bilateral agreement only provided traffic rights to airlines of the EU or Egypt. Even without a nationality clause, liberal Open Skies agreements tend to only provide fifth freedom rights—for example, the right for a U.S. carrier to fly from the U.S. to the EU and then continue to a third country. *See, e.g.*, Air Transport Agreement Between the Government of the United States of America and the Government of the Republic of Albania, U.S.-Alb., Annex 1 § 1, Sept. 24, 2003, *available at* <http://www.state.gov/documents/organization/114547.pdf> (requiring a U.S. point of origin for flights continuing from Albania to a third country). If the U.S. had negotiated for only fifth freedom rights with the third country, these fifth freedom rights with the third country would make seventh freedom rights with the EU meaningless since the former requires a U.S. origination or termination point.

<sup>190</sup> U.S.-EU Amended Agreement, *supra* note 82, art. 9.

<sup>191</sup> *See, e.g.*, Air Transport Agreement Between the Government of the United States of America and the Government of the United Arab Emirates, U.S.-U.A.E., art. 15, Mar. 11, 2002, *available at* <http://www.state.gov/documents/organization/114606.pdf>.



Because U.S. and EU airlines have instituted a number of business decisions in reliance on this agreement,<sup>192</sup> it seems unlikely that Open Skies rights between the U.S. and EU would suddenly be revoked.<sup>193</sup> Nevertheless, given the complexity of the U.S.-EU agreement and the many countries involved, any revocation could mean a loss of very beneficial rights to U.S. carriers.<sup>194</sup> Because the benefits that U.S. airlines receive from the U.S.-EU Open Skies agreement are so significant, any liberalization of U.S. foreign ownership restrictions should be directed at the EU.<sup>195</sup> The same benefits—namely, unrestricted U.S. carrier access to the same breadth of markets offered by the European community—are not available through the other Open Skies agreements currently signed by the U.S. The ability for U.S. carriers to offer unrestricted intra-European services is also an added benefit that other Open Skies agreements<sup>196</sup> with single nations typically do not offer. A U.S. agreement with a single nation does not produce the same access benefits as a U.S. agreement with a multinational community such as the EU.

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<sup>192</sup> US Airways, Continental Airlines, and Delta Air Lines, for example, have launched service to London Heathrow. Press Release, US Airways, US Airways Announces First Ever Service to London's Heathrow Airport (Nov. 20, 2007), <http://phx.corporate-ir.net/phoenix.zhtml?c=196799&p=irol-newsArticle&ID=1080176>; Press Release, Continental Airlines, Continental Airlines to Launch Twice-Daily Nonstop Flights to Heathrow From Both New York and Houston (Nov. 15, 2007), [http://phx.corporate-ir.net/phoenix.zhtml?c=85779&p=irol-newsArticle\\_Print&ID=1078367](http://phx.corporate-ir.net/phoenix.zhtml?c=85779&p=irol-newsArticle_Print&ID=1078367); Press Release, Delta Air Lines, Delta Customers Gain Nonstop Access to London-Heathrow, Paris-Orly and Lyon, France through Expanded Trans-Atlantic Partnership (Oct. 17, 2007), <http://delta.mediaroom.com/index.php?s=43&item=576>. Meanwhile airlines like Air France, Aer Lingus, and British Airways (through subsidiary "Open Skies") began operating transatlantic routes from EU member states other than their own. Press Release, Delta Air Lines, Delta Customers Gain Nonstop Access to London-Heathrow via Los Angeles, Complementing Service from Atlanta, New York-JFK (Dec. 11, 2007), <http://delta.mediaroom.com/index.php?s=43&item=485>; United Airlines Press Office, *supra* note 123 (regarding Aer Lingus); Robert Wall, *British Airways To Launch OpenSkies*, AVIATION WEEK (Jan. 9, 2008), [http://www.aviationweek.com/aw/generic/story\\_generic.jsp?channel=comm&id=news/OPEN01098.xml&headline=British%20Airways%20To%20Launch%20OpenSkies](http://www.aviationweek.com/aw/generic/story_generic.jsp?channel=comm&id=news/OPEN01098.xml&headline=British%20Airways%20To%20Launch%20OpenSkies).

<sup>193</sup> *Aeropolitics*, *supra* note 186 ("[S]ome . . . have expressed skepticism that either side would open an aviation trade war by suspending parts of the 2007 Agreement . . .").

<sup>194</sup> *Id.* DOT may have granted antitrust immunity to a transatlantic alliance in order to avoid a revocation of Open Skies rights. *Id.*

<sup>195</sup> See Cavinato, *supra* note 160, at 337 (recommending a three-pronged test to determine whether foreign investment restrictions should be loosened with respect to any particular nations). Cavinato's first prong requires that the nation with whom the U.S. loosens its restrictions (1) be a party to an Open Skies agreement with the U.S., and (2) provide U.S. citizens with reciprocal investment benefits in its airlines. *Id.* at 338–39.

<sup>196</sup> ASS'N OF EUROPEAN AIRLINES, *supra* note 186, at 2.

Additionally, the effectiveness of the U.S.-EU Open Skies agreement practically requires that foreign ownership liberalization be tailored to EU nations. If a non-EU entity were to acquire control of a U.S. airline, it is possible that the airline would lose its EU access privileges granted in the U.S.-EU Open Skies agreement.<sup>197</sup> A U.S. airline with an extensive route network in Europe could potentially be blocked from all of its EU destinations if a non-EU foreign entity—located in a country without an Open Skies agreement with the EU—took control of the U.S. airline. The potential for lost traffic rights has presented itself in a number of situations. Most recently, Russia threatened to ban Austrian Airlines from flying into Russia after Germany's Lufthansa acquired nearly 50% ownership in the airline.<sup>198</sup> Russia wanted the Austrian government, with whom it was engaged in a bilateral agreement, to “prove [Austrian Airlines] is still Austrian.”<sup>199</sup> Because of this potential scenario and the importance of EU route networks to U.S. airlines, the U.S. should limit foreign ownership to EU entities to gain the full benefits of the U.S.-EU Open Skies Agreement.

## *2. The EU's Commitment to Decreasing Government Influence and Subsidies in the Airlines*

The U.S.'s agreement with the EU also provides a more direct commitment to eliminating government interference and subsidies than other Open Skies agreements seem to include. While no Open Skies agreement directly speaks to the issue of government control or ownership of the airlines,<sup>200</sup> most agreements have precatory language that calls for “minimum government interference and regulation.”<sup>201</sup> Out of the twenty-five agreements observed in this Note, the U.S. agreement with India is the

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<sup>197</sup> Patel, *supra* note 10, at 511 (illustrating how traffic rights from the U.S. to the EU can be lost if the acquirer of a U.S. airline were from a country which did not have full traffic rights to the EU).

<sup>198</sup> Pilita Clark, *Russia Threatens Ban on Austrian Airlines*, FIN. TIMES, Mar. 1, 2010, at 1.

<sup>199</sup> *Id.*

<sup>200</sup> This determination is based on the review of twenty-five open skies agreements between the U.S. and other countries, including Canada, Chile, Ghana, Guatemala, Iceland, India, Indonesia, Jamaica, Japan (memorandum of understanding), Kuwait, Laos (draft), Liberia, Malaysia, Morocco, New Zealand, Nigeria, Pakistan, Panama, Qatar, Singapore, Switzerland, Tanzania, Thailand, and Turkey, as well as the U.S. agreement with the EU.

<sup>201</sup> See, e.g., Model Open Skies Agreement, U.S. Dep't of State 1 (2008), available at <http://www.state.gov/documents/organization/114970.pdf>.

only agreement to leave out this language,<sup>202</sup> while the agreement with Morocco calls for “minimum appropriate regulation.”<sup>203</sup> Regardless, these calls for minimum government interference do not have the force of law in Open Skies agreements.

Where the U.S.-EU agreement does provide more focus is in its anti-subsidy provisions. In fact, the agreement includes precatory language stating that the parties recognize “government subsidies may adversely affect airline competition,”<sup>204</sup> language that is not provided in other Open Skies agreements. Bearing greater legal weight is Article 14 of the agreement pertaining to government subsidies and support.<sup>205</sup> The provision plainly states, “The Parties recognise that government subsidies and support may adversely affect the fair and equal opportunity of airlines to compete in providing the international air transportation governed by this Agreement.”<sup>206</sup> As an enforcement mechanism, a party finding a breach of this provision can request a meeting of a joint committee, composed of members of both parties, to decide the matter<sup>207</sup> or it can approach government entities belonging to the breaching party diplomatically.<sup>208</sup>

In contrast, most other agreements mention the issue of subsidies only briefly as part of pricing provisions.<sup>209</sup> The pricing discussion is usually contained in Article 12 of the typical agreement,<sup>210</sup> which reads, “Each Party shall allow prices for air transportation to be established by each designated airline based upon commercial considerations in the marketplace. Intervention by the Parties shall be limited to . . . protection of airlines from

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<sup>202</sup> Air Transport Agreement Between the Government of the United States of America and the Government of India, U.S.-India, Apr. 14, 2005, *available at* <http://www.state.gov/documents/organization/114735.pdf>.

<sup>203</sup> Air Transport Agreement Between the Government of the United States of America and the Government of the Kingdom of Morocco, U.S.-Morocco, Oct. 10, 2000, T.I.A.S. No. 13,165, *available at* <http://www.state.gov/documents/organization/130941.pdf>.

<sup>204</sup> U.S.-EU Agreement, *supra* note 77, at 5.

<sup>205</sup> *Id.* art. 14.

<sup>206</sup> *Id.* art. 14(1).

<sup>207</sup> *Id.* art. 14(2); *see also id.* art. 18 (discussing the composition and procedures of the joint committee).

<sup>208</sup> *Id.* art. 14(3).

<sup>209</sup> The Model Open Skies Agreement does not mention government subsidies, but most agreements will include it as part of pricing provisions. Model Open Skies Agreement, *supra* note 201.

<sup>210</sup> In the U.S.'s agreement with Canada, the pricing provision, using similar language as that used in other agreements, is in article 6. Air Transport Agreement Between the Government of the United States of America and the Government of Canada, U.S.-Can., art. 6, Mar. 12, 2007, *available at* <http://www.state.gov/documents/organization/114887.pdf>.

prices that are artificially low due to direct or indirect governmental subsidy or support.”<sup>211</sup> The agreements specify “intervention” be provided in the form of consultations and direct communication with the offending party, with the desired outcome being a fair price on which both sides can agree.<sup>212</sup> If no agreement is reached, the allegedly problematic pricing continues in effect.<sup>213</sup> Although some enforcement against the use of subsidies exists in these provisions, the enforcement is primarily centered on the issue of unfair pricing and is relatively weak at best. If subsidies are found to result in unfair pricing, then the enforcement mechanisms can be triggered, though they may have little effect if the unfair pricing is allowed to continue. In a situation where subsidies do not result in pricing deemed unfair, however, no enforcement mechanisms are triggered at all.

The agreement between the U.S. and EU directly attacks the use of subsidies as they affect competition overall, not merely pricing.<sup>214</sup> The U.S.-EU agreement, in that sense, has more force in directly confronting the use of subsidies, and the joint committee, provided under Article 18 of the agreement, may have more control over the resolution of any subsidy problem entirely, not only from the perspective of unfair pricing. In other words, a party under the U.S.-EU agreement can complain about government subsidies of the other party, regardless of whether unfair pricing is experienced, and the resolution of the complaint is likely to tackle the very existence of the subsidy itself, not merely treating the unfair pricing effects of that subsidy. The U.S.-EU agreement is more likely to discourage the use of subsidies as a result.

### 3. *A Loss of Nationalism in EU Airlines*

Alongside the U.S. and EU’s written commitment toward minimizing government interference and subsidies, the landscape of the commercial

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<sup>211</sup> See, e.g., Air Transport Agreement Between the Government of the United States of America and the Government of Malaysia, U.S.-Malay., art. 12(1), Jun. 21, 1997, T.I.A.S. No. 12,871, available at <http://www.state.gov/documents/organization/114289.pdf>.

<sup>212</sup> See, e.g., Air Transport Agreement Between the Government of the United States of America and the Government of Qatar, U.S.-Qatar, art. 12(3), Oct. 3, 2001, available at <http://www.state.gov/documents/organization/114398.pdf> (“If either Party believes that any such price is inconsistent with the considerations set forth in paragraph (1) of this Article, it shall request consultations and notify the other Party of the reasons for its dissatisfaction as soon as possible.”).

<sup>213</sup> See, e.g., *id.*

<sup>214</sup> U.S.-EU Agreement, *supra* note 77, art. 14(2) (allowing recourse if one party finds that a government subsidy being provided to an airline of the other party adversely affects the “fair and equal opportunity of the airlines of the first Party to compete”).

airline industry in Europe also diminishes the likelihood of any government involvement. The landscape is now dominated by several large, privatized carriers, including airlines that are still considered national flag carriers as well as private low fare carriers. The flag carriers of Western European countries, in particular, have “achieved the highest or at least a sufficiently high degree of competitiveness,”<sup>215</sup> such that government protectionism through airline control or route restrictions is no longer needed. As a result, the nationalist protectionism smaller countries exhibit toward their airlines<sup>216</sup> is not as prevalent in Europe as it once was, making government interference in airline operations less likely.

In one sign that EU member states are no longer as protective of their home carriers, airline consolidation in the EU has resulted in several of the larger EU airlines taking ownership of smaller airlines from EU states other than their own. The Air France takeover of the Dutch airline KLM is one example, though KLM initially preserved its Dutch control and identity for traffic rights purposes.<sup>217</sup> The two entities still appear separate to the traveling public, but a single holding company owns both carriers.<sup>218</sup> In a similar fashion, Lufthansa has taken over Swiss International Air Lines<sup>219</sup> and heavily invested in Austrian Airlines,<sup>220</sup> Brussels Airlines,<sup>221</sup> and the United Kingdom’s British Midland International (bmi).<sup>222</sup> More recently, Spain’s Iberia Airlines and the U.K.’s British Airways signed a merger agreement of their two holding companies in 2010.<sup>223</sup> The fact that EU members are now willing to allow airlines from other member states to take

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<sup>215</sup> ZYLICZ, *supra* note 62, at 23.

<sup>216</sup> See *supra* notes 143–44 and accompanying text.

<sup>217</sup> Alistair Osborne & Henry Samuel, *Air France Agrees Takeover of KLM*, THE DAILY TELEGRAPH UK, Oct. 1, 2003, at 34, available at <http://www.telegraph.co.uk/finance/2864707/Air-France-agrees-takeover-of-KLM.html>.

<sup>218</sup> *Id.*

<sup>219</sup> LUFTHANSA, ANNUAL REPORT 2008, at 204 (2009).

<sup>220</sup> *Id.* at 4.

<sup>221</sup> *Id.*

<sup>222</sup> *Id.* at 7.

<sup>223</sup> Merger Project Between International Consolidated Airlines Group, S.A., Iberia, Lineas Aereas de Espana, S.A., and BA Holdco, S.A. 9–10 (June 2010), <http://phx.corporate-ir.net/External.File?item=UGFyZW50SUQ9NTIxMjd8Q2hpbGRJR D0tMXxUeXBIPtM=&t=1>. The trading of shares in each airline’s holding company ceased in January 2011, with new shares issued for the consolidated company, International Consolidated Airlines Group, S.A., and its primary listing on the London Stock Exchange. Steve Rothwell, *British Airways Strike Risk Looms as Ballot Overshadows Merger with Iberia*, BLOOMBERG (Jan. 19, 2011, 8:44 AM), <http://www.bloomberg.com/news/2011-01-19/british-airways-strike-risk-looms-as-ballot-overshadows-merger-with-iberia.html>.

over part or all of their home airlines highlights the fact that EU member governments are taking a more hands-off approach to airline governance. If any of these privatized EU carriers were to take control of a U.S. carrier, it would be unlikely that the government of the EU carrier would decide to exert any control.

The five largest airlines or airline groups based in the EU are Lufthansa, Air France-KLM, Ryanair, easyJet, and British Airways,<sup>224</sup> and all five are private carriers.<sup>225</sup> Based on size alone, they are the airline groups most likely to invest in U.S. carriers if presented the opportunity. Three of these groups—Lufthansa, Air France-KLM, and British Airways—and their subsidiaries were once national flag carriers in their own right, and were only privatized in the past several decades.<sup>226</sup> While these companies are now competitively the strongest carriers in Europe and have no need for government involvement, smaller flag carriers in Europe are also aiming for privatization. The Italian government, for example, allowed its national carrier Alitalia to be privatized despite political turmoil.<sup>227</sup> Nevertheless,

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<sup>224</sup> Based on 2009 figures. The Lufthansa group carried over 76.5 million passengers. *Investor Info 12/09 with Traffic Data for December*, LUFTHANSA INVESTOR RELATIONS, <http://investor-relations.lufthansa.com/fileadmin/downloads/en/financial-reports/traffic-figures/Lufthansa/2009/LH-Investor-Info-2009-12-e.pdf> (last visited Jan. 4, 2011). Air France-KLM carried nearly 71.4 million passengers. *Air France-KLM Financial Information*, AIR FRANCE-KLM FINANCE, <http://www.airfranceklm-finance.com/passenger-freight-traffic.html&navigationAnnee=2009> (last visited Jan. 4, 2011). Ryanair carried under 65.3 million passengers. *Passenger Traffic 2002/2011*, RYANAIR, <http://www.ryanair.com/en/investor/traffic-figures> (last visited Jan. 4, 2011). EasyJet carried under 46.1 million passengers. *EasyJet Monthly Traffic Statistics for December 2009*, EASYJET PLC, <http://corporate.easyjet.com/investors/monthly-traffic-statistics/2009/december.aspx> (last visited Jan. 4, 2011). British Airways carried over 31.8 million passengers during its financial year ending March 31, 2010. See *Preliminary Results [sic] for the Year to March 31, 2010*, INTERNATIONAL AIRLINES GROUP, <http://www.iagshares.com/phoenix.zhtml?c=240949&p=irol-newsArticle&ID=1497981&highlight=> (follow link for the full PDF file) (last visited Feb. 10, 2011).

<sup>225</sup> See AIR FRANCE-KLM, ANNUAL REPORT 2008–09, at 55 (2009); BRITISH AIRWAYS PLC., 2008/09 ANNUAL REPORT AND ACCOUNTS 61 (2009); EASYJET PLC, ANNUAL REPORT AND ACCOUNTS 2009, at 44 (2009); LUFTHANSA, ANNUAL REPORT 2008, at 30 (2009); RYANAIR LTD., ANNUAL REPORT 2009, at 101 (2009).

<sup>226</sup> See Colin Baker, *Air France-KLM Get Merger Approval*, FLIGHTGLOBAL (Jan. 6, 2004), <http://www.flightglobal.com/articles/2004/06/01/182217/air-france-klm-get-merger-approval.html> (discussing the French government's divestment of majority ownership in Air France); Kelley, *supra* note 165, at 553 (discussing how British Airways was privatized); *A Privatizing of Lufthansa*, N.Y. TIMES, Mar. 7, 1994, at D5 (noting how the German government would sell shares to become a minority owner of Lufthansa).

<sup>227</sup> Martial Tardy, *Alitalia Privatization Moving Smoothly*, AVIATION DAILY, Jan. 28, 2008, at 2; see also *Strike Hits Alitalia After Privatization*, N.Y. TIMES, Jan. 19, 2009,

some EU nations seeking privatization have been unsuccessful in doing so<sup>228</sup> or have renationalized their airlines.<sup>229</sup> Hungary is an example of an EU member state that renationalized its flag carrier to prevent the airline's collapse.<sup>230</sup> These smaller airlines are less likely to have the financial wherewithal to acquire controlling stakes in U.S. airlines, so even if U.S. foreign ownership restrictions were relaxed for all EU entities, the smaller, government-controlled airlines of Europe would be unlikely to acquire a U.S. airline or pose a threat to CRAF.

The relative financial weakness of smaller, state-owned EU airlines should be contrasted with the strength of airlines belonging to other nations where a foreign government is both a signatory of an Open Skies agreement and controls the dominant national carrier. In the latter situations, it may be possible for a foreign airline to have the financial resources and the interest in acquiring a controlling stake in a U.S. carrier. As one example, the government of Singapore,<sup>231</sup> through its holding company Temasek Holdings,<sup>232</sup> controls the city-state's flag carrier Singapore Airlines.<sup>233</sup> That airline acquired a 49% interest in the United Kingdom's Virgin Atlantic Airways (Virgin Atlantic).<sup>234</sup> If the EU's ownership restrictions were relaxed to allow foreign control, Singapore Airlines could purchase a controlling

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<http://www.nytimes.com/2009/01/19/business/worldbusiness/19iht-19alitalia.19485432.html> (discussing union action against the newly privatized Alitalia).

<sup>228</sup> See, e.g., Frank Lynch, *The Privatization of the Transportation Industry in Formerly Communist Countries: A Study of Poland and Hungary*, 48 ADMIN. L. REV. 559, 565–68 (1996) (discussing a long history of unsuccessful attempts to privatize the Polish carrier LOT Polish Airlines).

<sup>229</sup> See Brian Strauss, *Hungarian Government Reclaims Struggling Malev*, ATW DAILY NEWS (Mar. 2, 2010), <http://atwonline.com/airline-finance-data/news/hungarian-government-reclaims-struggling-malev-0427> (discussing the Hungarian government's rescue of Malev Hungarian Airlines in the form of reacquired ownership).

<sup>230</sup> *Id.*

<sup>231</sup> It should be noted that the U.S. has executed Open Skies agreements with both Singapore and Thailand, countries which are discussed *infra* in the text accompanying notes 232–37.

<sup>232</sup> *Temasek Holdings Factsheet*, TEMASEK HOLDINGS (Feb. 1, 2010), [http://www.temasekholdings.com.sg/pdf/Temasek%20Holdings%20Fact%20Sheet\\_update\\_010210.pdf](http://www.temasekholdings.com.sg/pdf/Temasek%20Holdings%20Fact%20Sheet_update_010210.pdf) (noting the Singaporean government's ownership of Temasek).

<sup>233</sup> SINGAPORE AIRLINES, LTD., ANNUAL REPORT 2008/09, at 215 (2009) (noting that Temasek Holdings owns 54.57% of Singapore Airlines' shares).

<sup>234</sup> *Id.* at 212. There is ongoing discussion about the possibility of Singapore Airlines selling its stake in Virgin Atlantic. See Chan Sue Ling, *Singapore Air New CEO May Shed Virgin Atlantic Stake*, BLOOMBERG BUSINESSWEEK (Jan. 5, 2011, 11:12 AM), <http://www.businessweek.com/news/2011-01-05/singapore-air-new-ceo-may-shed-virgin-atlantic-stake.html>.

stake in Virgin Atlantic, which would effectively result in Virgin Atlantic being owned by the Singapore government.

While the Singapore government may exert minimal interference in the operations of the businesses it owns,<sup>235</sup> other governments owning similarly large national flag carriers are not as deferential. Thai Airways International (THAI), for example, is frequently a target of Thai political interference. The state-controlled airline recently succumbed to political pressure from members of the government when it sought to discontinue service on particular domestic routes within Thailand, handing the routes over to its small, low-fare affiliate carrier, Nok Air.<sup>236</sup> Politicians whose home cities would have been affected by the route changes convinced THAI management to partially reverse its decision and to keep one daily domestic flight to Ubon Ratchathani, against better business judgment.<sup>237</sup> According to local observers, the fact that THAI partially reversed its business plans spoke “volumes about how political interference overrides [THAI’s] business decisions, and the airline’s vulnerability to the whims of politicians.”<sup>238</sup> If THAI were allowed to own and control a U.S. airline, it would therefore not be difficult to imagine the Thai government pressuring THAI and its U.S. affiliate to act according to its political will and counter to the needs of CRAF.

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<sup>235</sup> See Ho Ching, Executive Director and CEO, Temasek Holdings, Ltd., Address at the Institute of Policy Studies Corporate Associates Lunch: Temasek Holdings: Building Sustainable Value (Feb. 12, 2004), available at [http://www.temasekholdings.com.sg/news\\_room/press\\_speeches/12\\_02\\_2004.htm](http://www.temasekholdings.com.sg/news_room/press_speeches/12_02_2004.htm) (“[T]he government took care not to be involved in the business decisions of the government-linked companies . . . . This hands-off self-restraint enabled the Temasek companies to grow and thrive on sound commercial principles, unfettered by bureaucratic impositions or non-commercial government directives.”).

<sup>236</sup> Boonsong Kositchotethana, *THAI Bows to Pressure to Keep Ubon Route*, BANGKOK POST, Feb. 15, 2010, <http://www.bangkokpost.com/business/aviation/32939/thai-bows-to-pressure-to-keep-ubon-route>.

<sup>237</sup> *Id.* The Bangkok-Ubon Ratchathani route lost the carrier 74.9 million baht (roughly 2.3 million U.S. dollars) per year on average. *Id.*

<sup>238</sup> *Id.* The airline again came under scrutiny by government officials when the CEO proposed setting up a low cost subsidiary airline that would be minority-owned by a Singapore carrier with ties to the Singaporean government. Although much of the dispute was over the possibility of foreign control of a domestic airline, an issue that the U.S. DOT itself scrutinizes, statements by the Thai Transport Minister suggested that the ministry would scrutinize the deal based on the soundness of the business decision in addition to whether the airline would be placed under foreign control. Boonsong Kositchotethana & Amornrat Mahitthirook, *PM Patches Up Thai Tiger Row*, BANGKOK POST, Sept. 3, 2010, <http://www.bangkokpost.com/business/economics/194355/pm-patches-up-thai-tiger-row> (The Transport Minister stated, “As THAI (the airline) is under the ministry’s supervision, we reserve the right to put the issue under our scrutiny.”).



Other examples of state-controlled airlines with the resources to potentially acquire controlling stakes in U.S. airlines are Emirates<sup>239</sup> and Etihad<sup>240</sup> in the United Arab Emirates, and three of the largest air carriers in Africa: South African Airways,<sup>241</sup> EgyptAir,<sup>242</sup> and Royal Air Maroc<sup>243</sup> in Morocco. Within this list of countries, the U.S. has executed Open Skies agreements with the United Arab Emirates and Morocco. In Europe, several airlines remain state-owned, though they are relatively small players in their region. The largest among these are TAP Portugal,<sup>244</sup> Finnair,<sup>245</sup> Czech Airlines,<sup>246</sup> and LOT Polish Airlines.<sup>247</sup> All of these European carriers have the potential to acquire controlling interests in U.S. carriers with varying degrees of likelihood, but for the time being, their influence is overshadowed by the plethora of significantly larger, privatized carriers in Europe. Significant fiscal constraint resulting from economic weakness and

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<sup>239</sup> THE EMIRATES GROUP, ANNUAL REPORT 2008–2009, at 76 (2009).

<sup>240</sup> See *No Merger with Etihad, Emirates Says*, GULFNEWS.COM, Dec. 1, 2008, <http://gulfnnews.com/business/aviation/no-merger-with-etihad-emirates-says-1.147274> (noting that an Abu Dhabi bailout package did not involve a merger of government-owned Etihad Airways with Emirates). Etihad Airways has reportedly expressed interest in acquiring a stake in Virgin Atlantic. Steve Rothwell & Tamara Walid, *Virgin Atlantic Says Still in Early Stages of Assessing Future*, BLOOMBERG BUSINESSWEEK (Jan. 23, 2011, 10:30 AM), <http://www.businessweek.com/news/2011-01-23/virgin-atlantic-says-still-in-early-stages-of-assessing-future.html>.

<sup>241</sup> SOUTH AFRICAN AIRWAYS, 2009 ANNUAL REPORT: BUILDING ON RESTRUCTURING 59 (2009).

<sup>242</sup> See Ahmed Namatalla, *Soon Boarding*, BUSINESS TODAY EGYPT, Apr. 2006, <https://www.zawya.com/story.cfm/sidZAWYA20060411052834/Soon%20Boarding> (discussing the Egyptian government's decision to offer shares of Egyptair to the public).

<sup>243</sup> Mark Pilling, *Royal Air Maroc To Be Privatised: World Air Transport Forum News*, FLIGHTGLOBAL (Oct. 30, 2008, 1:44 PM), <http://www.flightglobal.com/blogs/airline-business/2008/10/royal-air-maroc-to-be-privatis.html> (discussing the Moroccan government's planned privatization of Royal Air Maroc). As of early 2010, there is no confirmation that the government has relinquished its controlling stake in the airline.

<sup>244</sup> GRUPO TAP, 2008 ANNUAL REPORT 100 (2009) (noting that the group's capital is provided by the Portuguese government).

<sup>245</sup> *Shareholders*, FINNAIR GROUP, [http://www.finnairgroup.com/investors/investors\\_4.html](http://www.finnairgroup.com/investors/investors_4.html) (last visited Mar. 25, 2011).

<sup>246</sup> CZECH AIRLINES, ANNUAL REPORT 2008, at 8 (2009).

<sup>247</sup> *Ownership Structure*, LOT POLISH AIRLINES, <http://www.lot.com/web/lot/proprietary-structure;jsessionid=2167D558BA885264792AD6D3E335577F.13> (last visited Jan. 4, 2011); see also Lynch, *supra* note 228 (discussing the history of attempts at privatizing LOT Polish Airlines).

government debt in Europe<sup>248</sup> has also diminished the likelihood that any European government-controlled entity—airline or otherwise—would seek to acquire a controlling stake in a U.S. airline.

#### 4. *The Existence of NATO and Its Possible Effects on CRAF Obligations*

The effect of state-control of foreign carriers in the EU is mitigated by the fact that many EU nations<sup>249</sup> are part of the North Atlantic Treaty Organization (NATO), a group whose multilateral treaty provides mutual defense protection to its signatories. When signing the North Atlantic Treaty (the treaty which forms NATO), the signatories agree, under Article 5, that “an armed attack against one or more of them . . . shall be considered an attack against them all.”<sup>250</sup> Once an attack is recognized, the signatories further agree to assist the attacked party and to take “such action as [they deem] necessary, including the use of armed force, to restore and maintain the security of the North Atlantic area.”<sup>251</sup> Ideally, governments of NATO member countries would therefore be expected to assist in U.S. military operations should the U.S. be attacked. If the foreign government indirectly controlling a U.S. carrier were a NATO member, it would arguably not hesitate to allow the U.S. carrier to meet its CRAF obligations, even if political forces in the NATO state opposed military involvement.<sup>252</sup>

In practice, however, NATO’s Article 5 has only been invoked once in the history of NATO—the September 11th terrorist attacks<sup>253</sup>—and during that one instance, the U.S. was directly attacked, a situation in which Article 5 clearly applies. CRAF, on the other hand, was activated most recently during the start of the 2003 Iraq War as part of Operation Iraqi Freedom,<sup>254</sup>

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<sup>248</sup> Alan Clendenning & Shawn Pogatchnik, *Gloom, Anger Spreads As European Economies Teeter*, WASH. TIMES, Nov. 24, 2010, <http://www.washingtontimes.com/news/2010/nov/24/ireland-unveils-4-year-plan-claw-back-20-billion/>.

<sup>249</sup> One exception of note is Finland, whose carrier is state-owned. *See supra* note 245.

<sup>250</sup> North Atlantic Treaty art. 5, Apr. 4, 1949, 63 Stat. 2241, 34 U.N.T.S. 243 [hereinafter NATO Treaty].

<sup>251</sup> *Id.*

<sup>252</sup> *See* Cavinato, *supra* note 160, at 339–42 (arguing that foreign entities from nations joining the U.S. in mutual defense pacts, like NATO, are more likely to honor CRAF obligations should they have control over U.S. carriers); *see also* IDA CRAF Study, *supra* note 132, at 45 (suggesting that national security treaties would strengthen CRAF commitments by U.S. carriers owned by foreign entities).

<sup>253</sup> Cavinato, *supra* note 160, at 340.

<sup>254</sup> *See supra* note 137 and accompanying text.

and since that war was not a result of a NATO member being directly attacked, Article 5 was never invoked. Although some NATO members partnered to provide military intervention to fulfill what they saw were the general purposes of NATO,<sup>255</sup> not all members felt obligated to assist the war effort. Some NATO members disagreed with the U.S.'s war policies in Iraq, particularly military action without approval from the United Nations Security Council,<sup>256</sup> and because their NATO commitment under Article 5 was not invoked, they were under no duty to participate. NATO members France, Belgium, Germany, and Turkey, for example, chose not to fully assist the U.S. at the outset of the Iraq conflict.<sup>257</sup> Had those states controlled U.S. carriers at the time of their opposition to the war, they had the potential to affect CRAF support for the war effort.

Despite the risks created by the Iraq War scenario, having the North Atlantic Treaty in place still provides some assurance that entities from NATO member nations will usually honor CRAF commitments should they gain control of a U.S. airline. All NATO members are likely to allow U.S. carriers under their control to participate in CRAF during times when Article 5 is invoked, and many members may still allow these same carriers to participate should the U.S. launch another military intervention similar to the Iraq War, depending on the circumstances.<sup>258</sup>

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<sup>255</sup> This includes purposes influenced by the precatory language in the North Atlantic Treaty, which recognizes that NATO members "are determined to safeguard the freedom, common heritage and civilisation of their peoples . . . . They seek to promote stability and well-being in the North Atlantic area." NATO Treaty, *supra* note 250. The language further states that the members "are resolved to unite their efforts for collective defence and for the preservation of peace and security." *Id.*

<sup>256</sup> Kerem Altıparmak, *Bankovic: An Obstacle to the Application of the European Convention on Human Rights in Iraq?*, 9 J. CONFLICT & SECURITY L. 213, 215 (2004); see also Jordan J. Paust, *Use of Armed Force Against Terrorists in Afghanistan, Iraq, and Beyond*, 35 CORNELL INT'L L.J. 533, 546 (2002) ("[Article 53 of the United Nations Charter] prohibits regional organizations [like NATO] from engaging in 'enforcement action under [the Security Council's] authority' without its authorization.").

<sup>257</sup> Jane Gilliland Dalton, *The United States National Security Strategy: Yesterday, Today, and Tomorrow*, 52 NAVAL L. REV. 60, 77-78 ("Turkey refused to permit U.S. forces to cross Turkish territory into Northern Iraq for Operation Iraqi Freedom . . . ."); Carsten Stahn, *Enforcement of the Collective Will After Iraq*, 97 AM. J. INT'L L. 804, 808 n.28 (2003) (listing several countries, including France, Belgium, and Germany, who vocally opposed the use of force in Iraq).

<sup>258</sup> This would assume that the U.S. would not wage war without the backing of some NATO partners.

### B. DOT Should Continue To Monitor Changes in Airline Ownership

Despite the aspirational goal of minimizing government interference, Open Skies agreements around the world, including the agreement between the U.S. and the EU, lack any language directly precluding the possibility of government ownership. The danger that a state-owned entity—whether in the EU or in another country—poses to the CRAF program in the event of foreign ownership liberalization must continue to be a factor in determining a U.S. airline's fitness for operations. For this reason, if foreign ownership restrictions were removed with respect to EU entities, DOT should continue to conduct studies of an airline's ownership and control. There are two possibilities that should raise concern: 1) if the U.S. were to relax ownership restrictions with respect to EU entities only, then DOT would need to ensure that the EU entity is not controlled by a non-EU entity, and 2) DOT needs to ensure that the EU entity is not controlled by a state government. Each of these concerns requires consistent attention to changes in the ownership structure of the foreign entity, as well as the political climate of the foreign country.

EU law provides that member states (or the nationals thereof) own at least 50% of any EU airline and that such states or nationals have effective control of the airline.<sup>259</sup> Assuming this law does not change and is effectively enforced by the EU, DOT should not have to worry about non-EU entities controlling those in the EU. If, however, the EU decided it wanted to loosen its restrictions to investors from other nations with which the EU had signed an Open Skies agreement, for example, then DOT would need to consider whether the change gives control of a U.S. airline to a non-EU foreign country.<sup>260</sup>

Of more concern is the second possible scenario: that an EU member state would re-exert control over its flag carrier, similar to how Malev Hungarian renationalized its airline as discussed *supra*.<sup>261</sup> EU member states could also temporarily gain ownership over their flag carriers to bail them out of financially difficult situations, especially if no private investors express any interest in the failing airline.<sup>262</sup> The moment such forms of

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<sup>259</sup> Regulation 1008/2008 of the European Parliament and of the Council of 24 September 2008 on Common Rules for the Operation of Air Services in the Community (Recast), art. 4(f), 2008 O.J. (L 293) 6.

<sup>260</sup> The Virgin Atlantic Airways and Singapore Airlines example, discussed *supra* in the text accompanying notes 231–34, illustrates this possibility.

<sup>261</sup> See Strauss, *supra* note 229.

<sup>262</sup> This was discussed as having occurred in Europe during the 1990s and in the U.S. as recently as the early 2000s with America West Airlines. See *supra* notes 169–73, and accompanying text.

nationalization or emergency ownership take place, DOT should review a U.S. carrier's ownership with ties to the EU member in question.

*C. The Distinction Between Cabotage and Increased Foreign Investment*

Any discussion involving a liberalization of foreign ownership restrictions should preclude the possibility for increased cabotage rights—that is, the right for a foreign airline to commercially operate U.S. domestic services. Foreign carriers in such a scenario would likely displace some U.S. carriers in the market, resulting in possible pressure for DOD to open up the CRAF program to those foreign carriers. CRAF commitments are likely enforceable in situations where a U.S. carrier is controlled by a foreign carrier; it is less certain that these same commitments would be enforceable against a participating foreign carrier—one that is registered and incorporated in a foreign country.<sup>263</sup> Foreign airlines, both public and private, can be influenced by their home governments.<sup>264</sup> Just as U.S. airlines are subject to U.S. regulations and potential U.S. government control, foreign carriers still fly subject to their home country's "sovereignty, regulatory authority, or influence,"<sup>265</sup> thereby weakening their commitments to CRAF even if they had earlier chosen to participate.

While it is still likely that foreign carriers operating domestic U.S. services will want to abide by their commitments to CRAF, it is less certain that they will ultimately fulfill those commitments when their home governments vehemently oppose a U.S. war effort.<sup>266</sup> As a possible form of enforcement, a foreign government could threaten to withhold the foreign airline's registration or certification to operate services if the airline chose to serve the U.S. military. In some cases, the foreign government may be able to seize or condemn the airline's aircraft. On the reverse side, U.S. airlines, even those controlled by foreign carriers, can be subject to a DOT revocation of their operating certification.<sup>267</sup> Without other recourse, U.S. airlines are strongly deterred from reneging on CRAF commitments by the fact that they may be forced out of operation.

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<sup>263</sup> See Cavinato, *supra* note 160, at 329–31 (discussing the debate over whether foreign carriers should be allowed to participate in CRAF).

<sup>264</sup> IDA CRAF Study, *supra* note 132, at 44 ("Just as governments grant or deny over-flight privileges or airport access privileges depending on international political considerations, they could be expected to deny or delay U.S. military use of aircraft owned by airlines under the influence or control of their citizens.").

<sup>265</sup> *Id.*

<sup>266</sup> See *supra* note 263 and accompanying text.

<sup>267</sup> See Cavinato, *supra* note 160, at 331 (noting how airlines incorporated in the U.S. are subject to U.S. regulatory control mechanisms).

DOT could revoke a foreign carrier's cabotage rights if the foreign carrier did not meet its CRAF obligations, though it is not certain whether this threat of revocation will actually deter the foreign carrier from reneging on its commitments. If the foreign carrier's operations in the U.S. are minimal, the foreign carrier can afford to discontinue these routes. If they are significant, the foreign carrier's home country could attempt to retaliate by revoking any access rights to U.S. carriers. This may weigh in the U.S.'s favor, as U.S. access to another country's domestic market is less likely to be as valuable as foreign access to the U.S. domestic market. Moreover, the revocation of a U.S. airline's access to a single international country will usually not make or break an airline's operations. Problematic situations will arise when a U.S. airline has large-scale operations in the foreign country in question, such that revocation of access rights will cripple the airline. Examples of these scenarios include Delta Air Line's operations in Amsterdam, Paris, and Tokyo.<sup>268</sup> Additionally, if multiple U.S. carriers serve the foreign country, the aggregate effect of shutting down direct access to that country may be significant. In the end, maintaining a set of U.S. incorporated airlines with U.S. registered aircraft to operate U.S. domestic services addresses accountability issues and avoids potential political problems presented by cabotage. Even if it is controlled by a foreign entity, a U.S. airline with a U.S. principal place of business and U.S. registered aircraft is still accountable to the U.S. government.

## V. CONCLUSION

The liberalization of foreign ownership restrictions is a fiercely political process involving a plethora of domestic and international actors, from members of Congress who must define these restrictions, to DOT who must interpret and apply these restrictions, to the Department of State and foreign governments, who must negotiate with these restrictions in mind. Through their actions in recent years, the Department of State and DOT have continued the liberalization of the airline industry at a cross border level, tempered by reasonable efforts to maintain U.S. national security and international fairness. Unfortunately, Congress's actions over the past decades have stifled this liberalization.

It is Congress's turn to catch up to the progress Executive Branch agency professionals have charted for it and to take a small step in a different direction. That step, of course, should not involve knocking completely down

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<sup>268</sup> See, e.g., Press Release, Delta Air Lines, Delta Air Lines Reports February Traffic (Mar. 4, 2010), <http://delta.mediaroom.com/index.php?s=43&item=962> (noting in its stock language for press releases that it considers Amsterdam, Paris, and Tokyo to be cities with Delta hub operations).

the wall to foreign investment, but, rather, it should involve a relaxation of restrictions where relaxation makes sense. Instead of opening up U.S. airlines to the world, investment should be opened up first to the EU only. Instead of ignoring any changes in ownership, DOT should continue what it is doing now: certifying an airline for operations only if the airline meets particular ownership requirements, including a bar on any control by foreign governments. In this way, the liberalization process can be managed in a fair and methodical way, sensitive to the needs of the country and of the airline industry.

